LIBRARY
SUPREME COURT, U. S.

JAN 18 1969

CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1968

No. 955

THE NATIONAL CASH REGISTER COMPANY, *Petitioner*,

v.

UNITED STATES OF AMERICA

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

PHILIP R. BECKER
COWDEN, PFARRER, CREW & BECKER
Winters Bank Building
Dayton, Ohio 45402

CHARLES E. MARTIN
JAMES E. RAMBO
Main and K Streets
Dayton, Ohio 45409

JOSEPH G. BLANDI
C. RUDOLF PETERSON
GEORGE W. BEATTY
LEE, TOOMEY & KENT
1200 18th Street, N. W.
Washington, D. C. 20036

PRESS OF BYRON S. ADAMS PRINTING, INC., WASHINGTON, D. C.

INDEX

	Page
Opinions Below	1
Jurisdiction	2
Question Presented	2
Treaty and Statutes Involved	2
Statement of the Case	5
Reasons for Granting the Writ	7
Conclusion	21
Appendix A	1a
Appendix B	11a

TABLE OF CITATIONS

CASES:

American Chicle Co. v. United States, 316 U.S. 450 (1942) 8, 10, 17, 18
Biddle v. Commissioner, 302 U.S. 573 (1938) 7, 11, 12, 14, 15, 17, 18, 19
Brantman v. United States, 167 F.Supp. 885 (N.D. Calif. 1958) ..... 15, n. 11
Dexter v. Commissioner, 47 B.T.A. 285 (1942) 18
Maximov v. United States, 373 U.S. 49 (1963) 19, 20

STATUTES, REGULATIONS AND RULINGS:

Finance Act of 1965, Eliz. 2, 1965, c. 25, Part IV ... 10, 20

Internal Revenue Code of 1954, 26 USC § 901 et seq., 68A Stat. 285:
§ 901 ..... 4, 6, 7, 9, 14
§ 902 ..... 4, 6, 7, 8, 9, 14, 15
§ 904 ..... 5, 18

28 U.S.C. 1254 2

28 U.S.C. 1346(a)(1) 6

Revenue Act of 1921, § 238(e), 42 Stat. 227, 259 .. 12, n. 7

Page

Revenue Act of 1938, § 131(f), 52 Stat. 447, 508 ..12, n. 7

Revenue Act of 1951, § 332(a), 65 Stat. 452, 506 ..12, n. 7

INCOME TAX REGULATIONS:

26 C.F.R. (Part 1), § 1.902-1(a), (d) 8

Rev. Rul. 56-289, 1956-1 Cum. Bull. 321 .....15, n. 11

Rev. Rul. 57-516, 1957-2 Cum. Bull. 435 9

I.T. 2762, XIII-1 Cum. Bull. 64 (1934) 9

O.D. 147, 1 Cum. Bull. 232 (1919) 9

MISCELLANEOUS:

United States-United Kingdom Income Tax Convention, 9 U.S. Treaties 1329:

Article I 2

Article XIII 2, 3, 6, 13, 14, 15, 16, 17, 20

Hearings Before a Subcommittee of the Committee on Foreign Relations, United States Senate, on Conventions With Great Britain and Northern Ireland respecting Income and Estate Taxes (79th Cong., 1st Sess.) .....12. nn. 8, 9

Sen. Exec. Rep. No. 6, 79th Cong., 1st Sess. .....12, n. 9

Owens, The Foreign Tax Credit (Cambridge 1961) 7, nn. 3, 4; 8; 9; 13; 15, n. 11; 19, n. 12

Taxation in the United Kingdom, World Tax Series, Harvard Law School (Cambridge 1957) .....11, n. 6

IN THE

Supreme Court of the United States

OCTOBER TERM, 1968

No.

THE NATIONAL CASH REGISTER COMPANY, *Petitioner,*

v.

UNITED STATES OF AMERICA

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

Petitioner prays that a writ of certiorari issue to review the decision of the United States Court of Appeals for the Sixth Circuit in this case.

OPINIONS BELOW

The findings of fact and opinion of the District Court (R. 13a-32a)[1] are reported at 270 F. Supp. 930. The opinion of the Court of Appeals (Appendix A, *infra*) is reported at 400 F.2d 820.

---

[1] Record references are to the separately bound Appendix C to the Government's brief in the Court of Appeals, now the separately bound Appendix C to this Petition.

JURISDICTION

The judgment of the Court of Appeals was entered on September 12, 1968, and a timely petition for rehearing was denied on October 23, 1968. (See Appendix B, *infra.*) The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTION PRESENTED

A United States corporate taxpayer received dividends in 1958 from its wholly-owned United Kingdom subsidiaries and elected, under Article XIII of the United States-United Kingdom Income Tax Convention, to take a direct foreign tax credit for the United Kingdom standard tax "appropriate to" those dividends. The question is whether the taxpayer may also take an indirect foreign tax credit under Sections 901 and 902 of the Internal Revenue Code for a fractional part of the remaining United Kingdom standard tax paid by the United Kingdom subsidiaries.

TREATY AND STATUTES INVOLVED

Income Tax Convention of April 16, 1945, between the United States and the United Kingdom, 60 Stat. 1377 (as amended by the Third Supplementary Protocol of August 19, 1957, 9 U.S. Treaties 1329, Art. II):

"ARTICLE I

"(1) The taxes which are the subject of the present Convention are:

"(a) In the United States of America:
The Federal income taxes, including surtaxes and excess profits taxes (hereinafter referred to as United States tax).

"(b) In the United Kingdom of Great Britain and Northern Ireland:
The income tax (including surtax), the excess profits tax and the national defense contribution (hereinafter referred to as United Kingdom tax).

"(2) The present Convention shall also apply to any other taxes of a substantially similar character imposed by either Contracting Party subsequently to the date of signature of the present Convention or by the government of any territory to which the present Convention is extended under Article XXII."

* * * * * * * * *

"ARTICLE XIII

"(1) Subject to Sections 901 to 905 of the United States Internal Revenue Code as in effect on the 1st day of January 1956, United Kingdom tax shall be allowed as a credit against United States tax. For this purpose

"(a) the recipient of a dividend paid by a corporation which is a resident of the United Kingdom shall be deemed to have paid the United Kingdom tax appropriate to such dividend, and

"(b) the recipient of any royalty or other amount coming within the scope of Article VIII of the present Convention shall be deemed to have paid any United Kingdom tax legally deducted from the royalty or other amount by the person by or through whom any payment thereof is made,

if the recipient of the dividend or royalty or other amount, as the case may be, elects to include in his gross income for the purposes of United States tax the amount of such United Kingdom income tax."

Sections 901, 902 and 904, Internal Revenue Code of 1954, as in effect on January 1, 1956, and for the year 1958, provide in part as follows (26 U.S.C. §§ 901, 902, 904; 68 A Stat. 285, 286):

"Sec. 901. *Taxes of Foreign Countries and of Possessions of United States.*

"(a) *Allowance of Credit.*—If the taxpayer chooses to have the benefits of this subpart, the tax imposed by this chapter shall, subject to the limitation of section 904, be credited with the amounts provided in the applicable paragraph of subsection (b) plus, in the case of a corporation, the taxes deemed to have been paid under section 902. * * *

"(b) *Amount Allowed.*—Subject to the limitation of section 904, the following amounts shall be allowed as the credit under subsection (a):

"(1) *Citizens and Domestic Corporations.*—In the case of a citizen of the United States and of a domestic corporation, the amount of any income, war profits, and excess profits taxes paid or accrued during the taxable year to any foreign country or to any possession of the United States;

* * * * * * *

Sec. 902. *Credit for Corporate Stockholder in Foreign Corporation.*

"(a) *Treatment of Taxes Paid by Foreign Corporation.*—For purposes of this subpart, a domestic corporation which owns at least 10 percent of the voting stock of a foreign corporation from which it receives dividends in any taxable year shall be deemed to have paid the same proportion of any income, war profits, or excess profits taxes paid or deemed to be paid by such foreign corporation to any foreign country or to any possession of the United States, on or with respect to the accumulated profits of such foreign corporation from which such dividends were paid, which the

amount of such dividends bears to the amount of such accumulated profits.

* * * * * * *

"(c) *Applicable Rules.*—

"(1) The term 'accumulated profits', when used in this section in reference to a foreign corporation, means the amount of its gains, profits, or income in excess of the income, war profits, and excess profits taxes imposed on or with respect to such profits or income; . . ."

* * * * * * *

"Sec. 904. *Limitation on Credit.*

"(a) *Limitation.*—The amount of the credit in respect of the tax paid or accrued to any country shall not exceed the same proportion of the tax against which such credit is taken which the taxpayer's taxable income from sources within such country (but not in excess of the taxpayer's entire taxable income) bears to his entire taxable income for the same taxable year."

STATEMENT OF THE CASE

In 1958, petitioner received substantial dividends, together with other income, from two wholly-owned United Kingdom subsidiaries referred to in the record as "NCR Ltd." and "NCR Mfg." The subsidiaries had paid United Kingdom standard tax, profits tax and other miscellaneous income taxes on their earnings.[2] (R. 14a-15a, 18a)

In its Federal income tax return for the year 1958, petitioner included in its income the amount of United Kingdom standard tax "appropriate to" the fore-

[2] Since there is no legal distinction for purposes of this case between the profits tax and the miscellaneous income taxes, subsequent references to the profits tax will also apply to the miscellaneous income taxes.

going dividends and then claimed a foreign tax credit for that amount of standard tax, pursuant to Article XIII of the Income Tax Convention between the United States and the United Kingdom (the "Convention"). Petitioner also claimed a foreign tax credit under §§ 901 and 902 of the Internal Revenue Code (the "Code") for a fractional part of the remaining standard tax and the profits tax paid by its United Kingdom subsidiaries. (R. 22a-23a)

Upon final audit of petitioner's return, the Internal Revenue Service concluded that if a foreign tax credit for the standard tax appropriate to the dividends was allowed under the Convention, no credit would be allowable under the Code for any of the remaining standard tax, although a credit would be allowable under the Code for a fractional part of the profits tax. The Internal Revenue Service recognized that its interpretation of the law would result in a smaller foreign tax credit, and hence a larger net United States tax, than if the credit were computed under the Code alone. (R. 34a) Accordingly, the Internal Revenue Service recomputed petitioner's tax without regard to the Convention, by eliminating from income the amount of standard tax which petitioner had reported in its return, and allowing a foreign tax credit under the Code for a fractional part of all of the standard tax and profits tax paid by petitioner's United Kingdom subsidiaries. (R. 25a-26a)

Petitioner paid the resulting deficiency in full and filed a claim for refund in due course. (R. 13a-14a) Following denial of its claim, petitioner filed a timely suit for refund pursuant to 28 U.S.C. 1346(a)(1). (R. 3a) The District Court upheld petitioner's claim in full (R. 28a-32a), but was reversed on appeal by the Court of Appeals (Appendix A, *infra*).

REASONS FOR GRANTING THE WRIT

The decision of the Court of Appeals is inconsistent with this Court's decision in *Biddle* v. *Commissioner*, 302 U.S. 573 (1938), and effectively deprives petitioner of the benefits of an international tax treaty between this country and the United Kingdom. The issue, which involves a pure question of law, is of importance to other United States corporations with subsidiaries operating in the United Kingdom. For all of these reasons, further review by this Court is warranted.

1. To understand why the decision below is inconsistent with this Court's decision in *Biddle*, it is necessary to review briefly the mechanics of the United States foreign tax credit system, the British standard tax system, and the Convention.

U. S. Foreign Tax Credit Rules:

United States individuals, and most other U. S. taxpayers, can obtain a foreign tax credit only for foreign taxes *actually* paid by the taxpayer in question.[3] However, there is a statutory exception to this rule in the case of a domestic corporation which owns at least 10% of the voting stock of a foreign corporation (referred to here as a "subsidiary") from which it receives dividends. On receipt of a dividend, the domestic corporation is treated in this situation *as if* it had paid certain foreign taxes actually paid by the foreign subsidiary.[4] Under §§ 901 and 902 of the Code (pp. 4-5, *supra*), the domestic company may take a credit for *both* its own foreign tax payments (the "direct"

---

[3] See § 901(b)(1) of the Code, p. 4, *supra*, and Owens, The Foreign Tax Credit (Cambridge 1961), p. 5 and Chapter 6.

[4] See §§ 901(a) and 902(a) of the Code, pp. 4-5, *supra*, and Owens, op. cit., pp. 9-11, and Chapter 3.

credit) *and* a share of of the foreign taxes paid by the foreign subsidiary (the "indirect" credit). Section 902(a) of the Code provides the basic formula for determining what portion of the total foreign tax paid by a foreign subsidiary may be claimed as an indirect credit by the domestic parent company on receipt of a dividend. As construed by this Court in *American Chicle Co.* v. *United States,* 316 U.S. 450 (1942), the applicable statutory language means that the parent receiving the dividend will be deemed to have paid foreign tax equal to:

$$\frac{\text{parent's dividend income}}{\text{subsidiary's "accumulated profits"}^{5}} \times \frac{\text{subsidiary's "accumulated profits"}}{\text{subsidiary's "total profits"}^{5}} \times \text{total foreign tax paid by subsidiary}$$

If the fractions are simplified by dividing out the factor consisting of the subsidiary's accumulated profits, the arithmetic result becomes:

$$\frac{\text{parent's dividend income}}{\text{subsidiary's total profits}} \times \text{total foreign tax paid by subsidiary}$$

This formula was changed by Congress in 1962 but it was effective for many years prior to that time, including 1958, the taxable year involved here. See Treasury Regulations § 1.902-1(a) and (d) (26 C.F.R. Part 1, § 1.902-1(a) and (d)); Owens, op. cit., pp. 102-106.

---

[5] In accordance with the terminology used in the record and §902 of the Code (p. 5, *supra*), the term "accumulated profits" will be used to designate the earnings remaining *after* the payment of foreign taxes and the term "total profits" will be used to designate the earnings *before* payment of such taxes.

The application of §§ 901 and 902 to a routine case where treaty relief is not available may be illustrated by assuming that in 1958 a U.S. parent corporation (P) owned all the stock of a foreign subsidiary (S). During that year, S had total profits of $1,000 on which it paid foreign income taxes of $400. Out of its accumulated profits of $600, it declared a dividend of $400 to P. Under the applicable foreign law, S was required to withhold on behalf of P a $40 tax on the dividend paid to P, so that P actually received a net dividend of only $360.

For U. S. tax purposes, a dividend withholding tax imposed by a foreign country on a U. S. shareholder is classified as a tax actually paid by the U. S. recipient of the dividend, even though the tax is remitted to the foreign government by the foreign subsidiary paying the dividend. In this situation, the foreign subsidiary does not pay tax on its own behalf, but acts instead as agent for the recipient of the dividend when it withholds the foreign tax due on the dividend. Thus, in the example above, P is entitled to a direct credit for the $40 withholding tax. However, since P is regarded as paying the tax, P must be treated as if it had actually received the full $400 dividend before paying out the $40 in tax. In other words, in order to claim the direct credit for the $40 withholding tax, P must include in income the declared dividend of $400, not just the net dividend of $360 which P actually received. Dividend withholding taxes have been treated in this fashion ever since the enactment of the first foreign tax credit provisions in 1918. See O.D. 147, 1 Cum. Bull. 232 (1919); I.T. 2762, XIII-1 Cum. Bull. 64 (1934); Rev. Rul. 57-516, 1957-2 Cum. Bull. 435; Owens, op. cit., pp. 111-112, 361-363.

Based on the foregoing, the computation of P's U. S. tax on the dividend would be as follows:

Total profits of S		$1,000
Foreign tax paid by S		400
Dividend income of P		400
Tentative U. S. tax of P at 52%		208
Direct credit for withholding tax on dividend	$40	
Indirect credit for taxes deemed paid (i.e., $400 dividend divided by $1,000 total profits, multiplied by foreign tax of $400)	160	
Total foreign tax credit		200
Net U. S. tax		8

The same example was used by the Government in its Court of Appeals brief (p. 12), and it is, therefore, undisputed that a corporation such as petitioner which receives dividends from a foreign subsidiary may take ***both*** a direct credit for 100% of any withholding taxes ***and*** an indirect credit for a fractional part of the foreign corporate taxes paid by the subsidiary, computed in accordance with the *American Chicle* formula.

The British Tax System:

Under the British standard tax system in effect prior to the Finance Act of 1965 (Eliz. 2, 1965 c. 25, Part IV), a British corporation paid standard tax on its profits in the year when earned. If a dividend was distributed to the shareholders, they included in income their pro rata share of the pre-tax corporate profits needed to pay such a dividend and then claimed a credit for the amount of standard tax payable on such

profits. The computations made by the shareholders were based on the standard tax rate in effect during the year of the distribution, even if this rate differed from the rate actually paid by the corporation on its profits. As pointed out by the Court of Appeals (Appendix A, p. 4a, n. 6), these rules meant that if a British corporation distributed $6 to a British shareholder in a year when the standard tax rate was 40%, the shareholder would report income of $10 and take a credit for $4. The $10 represents the pre-tax corporate profits needed to distribute a dividend of $6 after payment of a 40% tax, and the $4 represents the amount of such tax. In British terms, the $4 tax in the example is the amount of standard tax "appropriate to" the $6 net dividend received by the shareholder.[6]

Biddle and the Convention:

In the *Biddle* case, this Court held that a U. S. individual who received dividends from a British company was not entitled to a direct credit for the United Kingdom standard tax appropriate to his dividends, because he was not the "taxpayer" who paid the tax. Although British law treated the tax as one which was imposed on the shareholder, the Court concluded that the British corporation must be regarded as the taxpayer for U. S. purposes because the tax was levied, in the first instance, on the corporation's own profits. Since the Court based its decision on the ground that the shareholder was not the taxpayer for U. S. purposes, the decision made it totally impossible for individual U. S. shareholders to

[6] For a fuller explanation of the standard tax "appropriate to" a dividend, and the mathematical formula for computing such tax, see R. 16a-17a, *Biddle* v. *Commissioner*, *supra*, 302 U.S. at 575-577, 579-581 and Taxation in the United Kingdom, World Tax Series Harvard Law School (Cambridge 1957), pp. 257-258.

claim a foreign tax credit for the U. K. standard tax. Corporate shareholders were barred from obtaining a direct credit for the same reason, and under the then applicable rules, they could obtain an indirect credit only if they owned at least 50% of the voting stock of the British company.[7]

The *Biddle* decision represented a sharp break with prior practice. From 1918 until the mid-thirties, the Internal Revenue Service had treated the American shareholder as the party paying the U. K. standard tax, and had allowed the shareholder to claim a direct credit for the tax provided the amount of such tax was first included in the shareholder's income.[8] While the reversal of that position in the Biddle case was technically sound, the practical results of the new rule were harsh, and in recognition of this fact the scope of the *Biddle* decision was considerably narrowed by provisions included in the 1945 Income Tax Convention between the United States and the United Kingdom.[9]

---

[7] See §131(f) of the Revenue Act of 1938, 52 Stat. 447, 508. The 50% stock ownership requirement originated with §238(e) of the Revenue Act of 1921, 42 Stat. 227, 259, and remained unchanged until 1951 when the figure was lowered to the present 10% level by §332(a) of the Revenue Act of 1951, 65 Stat. 452, 506.

[8] See *Biddle* v. *Commissioner, supra,* 302 U.S. at 582, and *Hearings Before A Subcommittee Of The Committee on Foreign Relations, United States Senate, on Conventions with Great Britain and Northern Ireland respecting Income and Estate Taxes* (79th Cong., 1st Sess.) p. 70, reprinted in *Legislative History of United States Tax Conventions* (U.S. Government Printing Office 1962) Vol. 2, p. 2583 at p. 2636.

[9] See Hearings, note 8, *supra;* Sen. Exec. Rep. No. 6, 79th Cong., 1st Sess., p. 11, reprinted in *Legislative History,* note 8, *supra,* p. 2651 at p. 2661.

The relevant portion of the 1945 Convention, as slightly modified by a 1957 supplementary protocol, reads as follows (p. 3, *supra*):

> "Subject to Sections 901 to 905 of the United States Internal Revenue Code as in effect on the 1st day of January 1956, United Kingdom tax shall be allowed as a credit against United States tax. For this purpose . . . the recipient of a dividend paid by a corporation which is a resident of the United Kingdom shall be deemed to have paid the United Kingdom tax appropriate to such dividend . . . if the recipient . . . elects to include in his gross income for the purposes of United States tax the amount of such United Kingdom income tax."

The parties agree that the term "United Kingdom tax appropriate to such dividend" refers to the standard tax appropriate to the dividend, determined in accordance with British law. (R. 17a)

In substance, if Convention relief is elected, the standard tax appropriate to the dividend is treated exactly like a dividend withholding tax. See Owens, op. cit., p. 366, n. 16, and pp. 372-373. The recipient of the dividend is treated as if he had received the full amount of the pre-tax dividend ($10 in the example on p. 11, *supra*) and then paid the foreign tax due on it ($4 in the example), thereby ending up with an amount of cash equal to the net dividend actually received ($6 in the example). In accordance with this approach, the full amount of the $10 pre-tax dividend is includable in the recipient's income for U. S. tax purposes, and a direct credit may be claimed for the $4 of standard tax withheld from that dividend. This is precisely the way in which regular dividend withholding taxes are treated.

(See p. 9, *supra*.) Consequently, by reason of the Convention, the direct credit allowable for the standard tax appropriate to the dividend is the same as it was prior to the *Biddle* decision. (See p. 12, at n. 8, *supra*.)

While Article XIII of the Convention treats the standard tax appropriate to the dividend as a withholding tax, nothing whatever is said about the remaining standard tax paid by the British company, or about other U. K. income or profits taxes. Petitioner contends, and the District Court held (R. 31a), that the remaining standard tax must be treated under the *Biddle* decision as a corporate income tax paid by the British corporation. Thus, it falls into the same category as the profits tax paid by the British company. Under §§ 901 and 902 of the Code, an American corporation owning 10% or more of the stock of the British company is therefore entitled, when it receives a dividend, to claim an indirect credit for the proper fractional part of those U. K. taxes.

In its brief in the Court of Appeals (p. 9, n. 5 and p. 28), the Government agreed that, if petitioner was allowed a direct credit pursuant to the Convention for the standard tax appropriate to the dividend, petitioner could also take an indirect credit for the proper fractional part of the profits tax paid by its U. K. subsidiaries. However, the Government contended, and the Court of Appeals held, that petitioner could not take an indirect credit for any part of the remaining standard tax paid by petitioner's U. K. subsidiaries.

In so holding, the Court of Appeals did not challenge petitioner's assertion that under the Convention, the standard tax appropriate to a dividend must be treated as a dividend withholding tax imposed directly on the

recipient of the dividend.[10] Nor did the Court of Appeals deal directly with petitioner's assertion that the remaining standard tax is not covered by Article XIII of the Convention and must therefore continue to be treated under the *Biddle* case as a corporate tax imposed on the foreign subsidiary paying the dividend.[11] Instead, the Court of Appeals based its decision on the premise that, if a direct credit is allowed under the Convention for the amount of standard tax which is appropriate to the dividend under British law, "the taxpayer's use of a § 902 [indirect] credit for the remaining standard tax results in a credit for foreign tax allocable to earnings which were not distributed as dividends" (Appendix A, p. 9a). Since the Court of Appeals regarded this as an impermissable result in view of the overall purpose of the foreign tax credit provisions, the Court held that no indirect credit could be taken for any part of the standard tax if a direct credit was claimed under the Convention.

We submit that this analysis makes a nullity of the *Biddle* decision in any case where a corporate shareholder elects Convention relief. In fact, there is no justi-

---

[10] Since individuals are permitted to claim credit only for foreign taxes actually paid by them (p. 7, *supra*), the undisputed fact that individuals may credit the standard tax appropriate to the dividend under Article XIII is proof that this tax is regarded for U. S. tax purposes as having been imposed on the shareholder receiving the dividend, rather than the foreign corporation paying it, if treaty relief is elected.

[11] Because the Convention "does not revoke the principle of the [*Biddle*] case which is still effective except in the particular situation covered by the treaty" (Owens, op. cit., p. 366), the portion of the standard tax to which Article XIII does not apply must still be regarded as a British corporate tax. *Cf.* Rev. Rul. 56-289, 1956-1 C.B. 321 and *Brantman* v. *United States*, 157 F.Supp. 885 (N.D. Calif. 1958).

fication for doing so, because the statute permits corporate stockholders to take direct and indirect credits simultaneously.

Since the standard tax appropriate to the dividend is regarded under the Convention as a tax actually paid by the recipient of the dividend (n. 10, *supra*), allowance of a *direct* credit for that tax cannot affect the calculation of the *indirect* credit which relates solely to the foreign taxes paid by the foreign subsidiary. Moreover—and this is most important—the calculation of the amount of standard tax appropriate to the dividend which may be credited under the Convention has nothing to do with the amount of tax actually paid by the British corporation on the earnings distributed as a dividend. For example, suppose that an American shareholder owns all the stock of a British corporation. In Year 1, the corporation has $100 of earnings which are subjected to standard tax at the rate of 40%, leaving the corporation with after-tax earnings of $60. In the following year, when the standard tax rate has gone up to 50%, the corporation distributes half of its accumulated Year 1 earnings, or $30. The standard tax *actually* paid on the distributed earnings is $20 (i.e., half of the $40 tax actually paid). However, since the shareholder is entitled under the Convention to claim a credit at the *current* standard tax rate, the shareholder will be able to take a credit of $30, which is the amount of standard tax appropriate to a $30 net dividend at a 50% rate. (See R. 16a-17a). The direct credit of $30 allowable under the Convention will therefore exceed the $20 of tax actually paid on the distributed earnings. In its brief (p. 22, fn. 25) and reply brief (p. 5, fn. 3) in the Court of Appeals, the Government conceded that this is the effect of Article XIII.

In its opinion (Appendix A, pp. 8a, 9a) the Court of Appeals suggests that the only purpose of Article XIII is to avoid double taxation, and that consequently, a claimed credit should not be allowed where "there is no danger of international double taxation". Obviously, however, the effect of the Convention is broader than the Court's opinion indicates, because it is possible, as shown above and conceded by the Government, to get credits under the Convention alone for amounts in *excess* of the total foreign tax actually paid on the distributed earnings. Taxpayer is not here claiming such credits, but the point is significant because it clearly proves that Convention relief was intended to extend to cases where there was no danger of double taxation at all.

Because Article XIII of the Convention applies only to the standard tax "appropriate to" the dividend, the remaining standard tax retains its character under *Biddle* as a British corporate tax, and is therefore eligible for the indirect credit. Although the Court of Appeals' opinion indicates that this would result in allowing a credit for taxes "allocable to earnings which were not distributed as dividends" (Appendix A, p. 9a), the opinion fails to mention the stipulated fact (R. 22a-23a) that the formula prescribed by this Court in the *American Chicle* case, *supra,* was used in calculating the indirect credit claimed by petitioner in the present case. The whole point of that formula is to limit the indirect credit to the amount of foreign corporate tax allocable to the distributed earnings, and the formula has that effect in the present case.

If the dividends received by petitioner from its British subsidiaries in 1958 had been subject to an actual withholding tax of 38.75% (the standard tax rate in

effect in 1958), petitioner would unquestionably have been entitled to take a direct credit for 100% of the withholding tax, plus an indirect credit for a fractional part (determined in accordance with the *Chicle* case) of the remaining U. K. taxes paid by the British subsidiaries. (See p. 10, *supra*). While no withholding tax, as such, was actually imposed in 1958, the Convention has the effect of treating the amount of standard tax appropriate to the dividends at the 38.75% rate as though such tax were a withholding tax. Accordingly, petitioner claimed (R. 22a, 16a-18a), and is entitled to, a direct credit for that amount of tax. Under *Biddle*, the remaining standard taxes, along with the profits taxes paid by the U. K. subsidiaries, are eligible for the indirect credit, just as they would be if an actual 38.75% withholding tax had been imposed. Of course, petitioner is not entitled to an indirect credit for the full amount of the remaining taxes, and has not claimed such a credit. On the contrary, petitioner has claimed an indirect credit only for the fractional portion of those taxes attributable to the dividends it received, determined in accordance with the *Chicle* case. (R. 22a-23a)

The implication in the Court of Appeals' opinion that allowance of combined direct and indirect credits in this fashion would produce an excessive overall credit is dispelled by the stipulated fact (which is not mentioned in the Court's opinion) that the combined credits claimed by petitioner were within the limitation established by § 904 of the Code. (R. 27a). Since the purpose of the § 904 limitation is to prevent the credit for taxes paid to a foreign country from being used to eliminate the U. S. tax on income received from other sources (*Dexter* v. *Commissioner*, 47 B.T.A. 285, 291 (1942), *acq.* 1948-2 C.B. 1), a claimed credit which admittedly

falls within the limitation can scarcely be termed excessive.

2. The effect of the Court of Appeals' decision is to deprive petitioner, and other similarly situated corporate taxpayers, of the benefits afforded by a tax convention which this Court has described as "a solemn treaty between this Nation and a foreign sovereign". *Maximov v. United States*, 373 U.S. 49, 54 (1963). If a taxpayer-corporation which elects to claim a direct credit under the Convention thereby loses its right to take an indirect credit for standard tax under the Code—which is what the Court of Appeals held—the end result for the taxpayer will normally be a smaller credit and a greater net U.S. tax than if the taxpayer had ignored the Convention and claimed an indirect credit under the Code alone. This was true in the present case, and in order to avoid penalizing petitioner for claiming a Convention credit, the Internal Revenue Service had to recompute petitioner's credit under the Code alone. (R. 34a, R. 25a-26a). In short, under the Government's theory and the decision of the Court of Appeals, it would have been a burden rather than a benefit to petitioner to have its foreign tax credit computed under the Convention and Code combined.[12]

As previously stated, the *Biddle* decision made it impossible for many U.S. taxpayers to claim any credit at all for the U.K. standard tax, but even under *Biddle*, corporate stockholders owning at least 50% of the vot-

[12] Under certain fortuitous circumstances, some of which are described in Owens, op. cit., pp. 370-371, claiming a Convention credit could benefit the taxpayer even under the approach taken by the Government and the Court of Appeals. However, we can find nothing in the legislative history of the Convention to suggest that the Convention was intended to furnish relief only in these limited circumstances.

ing stock of a British subsidiary were still in a position to claim an indirect credit for U.K. standard tax under the Code. (See p. 12, *supra*, at n. 7). As a theoretical matter, the negotiators of the Convention might therefore have decided that Article XIII relief should not be extended to corporate taxpayers like petitioner who were already entitled to claim an indirect credit for the full amount of U.K. tax under the Code. Alternatively, the negotiators might have decided to give such taxpayers the option of using Article XIII or the Code, but not both. In point of fact, however, the negotiators did neither of these things. It follows, therefore, that the Convention was designed to afford corporate taxpayers such as petitioner additional relief above and beyond the indirect credit which they could already obtain under the Code alone.[13] The relief intended by the negotiators of the Convention can be afforded by applying the Convention according to its plain terms, without reading in implied limitations as the Court of Appeals did. *Cf. Maximov* v. *United States, supra.* It follows that petitioner is entitled to claim Article XIII relief for the portion of the U.K. tax to which that Article relates without foregoing its right to take a regular indirect credit under the Code for the remaining U.K. tax.

3. Because the Finance Act of 1965 (p. 10, *supra*) changed the method of taxing British corporations, the issue presented here will not arise under current law. Nevertheless, the issue has current significance. We are advised that other United States corporate taxpayers

[13] To obtain such relief, the taxpayer must pay a partial price by including in income the amount of standard tax credited under the Convention—an amount which would not be includable in income if a credit were claimed under the Code alone. Petitioner paid this intended price by including the amount of such tax in its reported income. (R. 22a)

with United Kingdom subsidiaries have the question pending for prior years which are still open under the statute of limitations, and in view of the considerations previously discussed, we therefore believe that the question is one which merits further review by this Court.

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari in this case should be granted.

Respectfully submitted,

PHILIP R. BECKER
COWDEN, PFARRER, CREW & BECKER
Winters Bank Building
Dayton, Ohio 45402

CHARLES E. MARTIN
JAMES E. RAMBO
Main and K Streets
Dayton, Ohio 45409

JOSEPH G. BLANDI
C. RUDOLF PETERSON
GEORGE W. BEATTY
LEE, TOOMEY & KENT
1200 18th Street, N. W.
Washington, D. C. 20036

APPENDIX A

No. 18109

UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

NATIONAL CASH REGISTER CO., *Plaintiff-Appellee,*
v.
UNITED STATES OF AMERICA, *Defendant-Appellant.*

APPEAL from the United States District Court
for the Southern District of Ohio.

Decided September 12, 1968.

Before O'SULLIVAN and PHILLIPS, Circuit Judges, and CECIL, Senior Circuit Judge.

PHILLIPS, Circuit Judge. During 1958 National Cash Register Company, a Maryland corporation with its principal place of business in Dayton, Ohio, owned all of the voting stock of two subsidiary corporations, The National Cash Register Company Limited (NCR Ltd.) and The National Cash Register (Manufacturing) Limited (NCR Mfg.). Both of the subsidiaries were organized under the laws of and were operated in the United Kingdom.

The issue in this case is whether, with respect to standard tax paid by a United Kingdom subsidiary, a United States corporation which received dividends in 1958[1] from a wholly owned United Kingdom subsidiary is entitled to a foreign tax credit under both § 902 of the Internal Revenue Code[2] and Article XIII(1) of the United States-United

---

[1] The year in which the dividends were received is pertinent to the issue, because there would be no occasion to claim multiple credits under present British tax law.

[2] "Sec. 902. *Credit for Corporate Stockholder in Foreign Corporation.*

"(a) *Treatment of Taxes Paid by Foreign Corporation.*—For purposes of this subpart, a domestic corporation which owns at least 10 percent of the voting stock of a foreign corporation from which it receives dividends in any taxable year shall be deemed to have paid the same proportion of any income, war profits, or excess

Kingdom Income Tax Convention of 1945, as amended.[3] The District Court held that the taxpayer corporation was entitled to take a credit for the standard tax under both § 902 and the Tax Convention and entered judgment in favor of the taxpayer and against the Government for a refund of $508,643.65 plus interest of $96,263.84. The Government appeals, contending that provisions of § 902 and Article XIII(1) are mutually exclusive and that the taxpayer is not entitled to a credit under both with respect to the standard tax.

---

profits taxes paid or deemed to be paid by such foreign corporation to any foreign country or to any possession of the United States, on or with respect to the accumulated profits of such foreign corporation from which such dividends were paid, which the amount of such dividends bears to the amount of such accumulated profits.

* * * * * * * *

"(c) *Applicable Rules.*—

"(1) The term 'accumulated profits', when used in this section in reference to a foreign corporation, means the amount of its gains, profits, or income in excess of the income, war profits, and excess profits taxes imposed on or with respect to such profits or income; . . ."

[3] "ARTICLE XIII

"(1) Subject to Sections 901 to 905 of the United States Internal Revenue Code as in effect on the 1st day of January 1956, United Kingdom tax shall be allowed as a credit against United States tax. For this purpose

"(a) the recipient of a dividend paid by a corporation which is a resident of the United Kingdom shall be deemed to have paid the United Kingdom tax appropriate to such dividend and

"(b) the recipient of any royalty or other amount coming within the scope of Article VIII of the present Convention shall be deemed to have paid any United Kingdom tax legally deducted from the royalty or other amount by the person by or through whom any payment thereof is made,

if the recipient of the dividend or royalty or other amount, as the case may be, elects to include in his gross income for the purposes of United States tax the amount of such United Kingdom income tax."

THE BRITISH DIVIDEND TAX

In order to answer the question presented it is necessary to understand some of the principles of British taxation of corporate dividends. The two subsidiary corporations were subject to the United Kingdom standard tax, an income tax imposed at the flat rate of 38.75 per cent. As British corporations, both subsidiaries were also subject to a profits tax levied at the rate of ten per cent. The standard tax applies both to individuals and to corporations. The profits tax applies only to corporations. Neither tax is deductible in computing the other.

In 1958 both subsidiaries paid dividends "free of standard tax" to the parent corporation. In the United Kingdom a corporate dividend may be declared either "free of standard tax" or "with deduction of standard tax."[4] These United Kingdom tax concepts have no parallel in the tax treatment of dividends by the United States.

A British corporation pays dividends out of profits from which standard tax and profits tax already have been deducted. When a dividend is declared "free of standard tax," it means (1) that the declared amount of the dividend is actually paid to the shareholder and (2) that the dividend is not subject to any additional United Kingdom tax after it has been paid to the shareholder.[5] When the shareholder is reporting his income, however, he is required to include the amount of the dividend actually received plus an amount representing the proportional share of the stand-

---

[4] The distinction between a dividend "free of standard tax" and a dividend "with deduction of standard tax" is of no consequence. In *Biddle* v. *Commissioner*, 302 U.S. 573, 580, Mr. Justice Stone said: "The differences in the two methods of deduction are to be found only in the formal bookkeeping data which, in the British system, are communicated to the stockholders, . . ."

[5] However, an individual shareholder is subject to a surtax on a dividend "free of standard tax" if his income reaches a certain level. A corporation is not subject to the surtax.

ard tax that the corporation has paid on the earnings from which the dividend was distributed.[6] In British tax nomenclature the phrase "standard tax appropriate to the dividend" refers to the pro rata share of the standard tax which the corporation has paid on the earnings from which the dividend was paid. A corporation is treated as a conduit composed of its shareholders. Although the shareholder reports the dividend actually received plus the standard tax appropriate to the dividend, the shareholder is not subject to any tax on the dividend. "The scheme of the British legislation is to impose on corporate earnings only one standard tax, at the source, and to avoid the 'double' taxation of the corporate income as it passes to the hands of its stockholders, . . ." *Biddle* v. *Commissioner, supra*, 302 U.S. 573, 579.

THE TAX CONVENTION

Because of the decision in *Biddle* v. *Commissioner, supra,* 302 U.S. 573, a special treaty provision was deemed necessary to afford United States stockholders a foreign tax credit for the standard tax appropriate to the dividend received from a United Kingdom corporation. In *Biddle* the Supreme Court held that for purposes of United States taxation the standard tax appropriate to the dividend was a tax imposed on the British corporation, not a tax imposed on the recipient of the dividend. Having characterized the standard tax as a tax imposed upon and collected from the corporation, the Court found that a shareholder was not warranted in taking a credit for a tax which he did not pay.

Article XIII(1) of the Tax Convention provides that if the shareholder of the United States receiving a dividend paid by a British corporation elects to include in his gross income the amount of the standard tax appropriate to the

---

[6] For example: If a British corporation declared a dividend of $6.00 "free of standard tax" and if the standard tax were imposed at the rate of 40 per cent, the shareholder would have to report $10.00, representing $6.00 for the dividend received and $4.00 for the standard tax appropriate to the dividend.

dividend, the recipient will be deemed to have paid the standard tax appropriate to the dividend. Accordingly, the shareholder who complies with the inclusion requirement of Article XIII(1) is allowed a direct credit against his United States tax for the amount of the standard tax appropriate to the dividend. It is to be emphasized that the foreign tax credit provided by Article XIII(1) is limited to the standard tax appropriate to the dividend. No credit is available under Article XIII(1) for the standard tax which is allocable to the portion of the corporate earnings which are not distributed as dividends. Nor does Article XIII(1) offer a foreign tax credit for other United Kingdom taxes such as the profits tax.

SECTION 902, INTERNAL REVENUE CODE

Section 902 permits a domestic corporation owning at least ten per cent of the voting stock of a foreign corporation from which it receives dividends in any taxable year to take a credit for a fractional portion of the taxes paid by the foreign corporation. Unlike Article XIII(1), which limits the credit to the standard tax paid by the corporation, § 902 provides a credit for "any income, war profits or excess profits taxes" paid by the foreign corporation. In *American Chicle Co.* v. *United States*, 316 U.S. 450, the Supreme Court established the formula for the § 902 credit for taxes deemed to have been paid on profits distributed as dividends. The numerator is the dividends received by the parent corporation. The denominator is the accumulated profits of the foreign subsidiary corporation. The multiplicand is the taxes paid upon or with respect to the accumulated profits of the foreign corporation: i.e., "so much of the taxes as is properly attributed to the accumulated profits, or the same proportion of the total taxes which the accumulated profits bear to the total profits." 316 U.S. at 452.[7]

---

[7] This formula is set forth in its fractional form in 5 Mertens, Law of Federal Income Taxation, § 33.14 (rev. 1963).

It is important to note that § 902 limits the credit for foreign taxes to that proportion of the tax which the dividend received by the domestic corporation bears to the total profits of the foreign corporation. Although the foreign corporation may have paid foreign taxes in a given year, under § 902 the domestic corporation is not entitled to any credit for those foreign corporation taxes for a year in which it receives no dividends from the foreign corporation. *Abbot Laboratories International Co.* v. *United States*, 160 F. Supp. 321, 328 (N.D. Ill.), aff'd per curiam, 267 F.2d 940 (7th Cir.).

THE CLAIM FOR DOUBLE CREDITS

Coming now to the factual details of the present case, the two subsidiaries during 1958 had total profits before payment of taxes and accumulated (after tax) profits as follows:

	Total profits	Accumulated profits
NCR Ltd.	$2,409,564.52	$1,235,244.93
NCR Mfg.	3,927,833.75	1,886,861.66
Total:	$6,337,398.27	$3,122,106.59

The 1958 taxes paid by the subsidiaries were as follows:[8]

	United Kingdom		Miscellaneous	
	Standard Tax	Profits Tax	Foreign Income Taxes	Total Tax
NCR Ltd.	$ 961,654.96	$207,583.57	$5,081.06	$1,174,319.59
NCR Mfg.	1,705,578.99	335,393.10		2,040,972.09
Total:	$2,667,233.95	$542,976.67	$5,081.06	$3,215,291.68

[8] NCR Ltd. was also subject to certain income taxes imposed by countries other than the United Kingdom or the United States which for the purposes of the § 904 limitation on the amount of the foreign tax credit are deemed to have been paid to the United Kingdom.

Out of the accumulated profits remaining after payment of the foregoing taxes, the two subsidiaries paid certain dividends to the taxpayer. The taxpayer also received certain other income from NCR Mfg. These amounts were as follows:

	Accumulated profits	Dividends declared and received	Other income
NCR Ltd.	$1,235,244.93	$1,019,190.01	
NCR Mfg.	1,886,861,66	1,571,981.25	$1,693,857.13
Total:	$3,122,106.59	$2,591,171.26	$1,693,857.13

The dividends received by the taxpayer were declared "free of standard tax."

The District Court allowed the taxpayer's computation which (1) took a direct credit under Article XIII(1) for the standard tax appropriate to the dividend plus (2) an indirect credit under § 902 for the remaining standard tax which was allocable either to earnings which were retained after the payment of dividends or to earnings which were used to pay United Kingdom profits tax.[9] In determining whether a credit for standard tax appropriate to the dividend may be taken under Article XIII(1) and another credit taken under § 902 for the remaining standard tax, we are faced with a situation in which neither the express language nor the published history of the Code or the Tax Convention provides definitive guidance.

The taxpayer contends that Article XIII(1) treats the standard tax appropriate to the dividend as a withholding tax and that under *Biddle* the remaining standard tax must be treated as a corporate income tax paid by the British

[9] The reason that some of the standard tax was allocable to the payment of profits tax is that the standard tax is not deducted in the computation of the profits tax.

subsidiary corporations. Following this reasoning, the District Court said: "Article XIII does not say or imply that only a part of the United Kingdom tax should be allowed as a credit and the Court can find no reason for doing so." We cannot agree.

The purpose of the Code and of the Convention is to avoid the incidence of double taxation by different nations of the same dividends. The avowed purpose of the Tax Convention is the "avoidance of double taxation and the prevention of fiscal evasion." [10] Explaining the purpose of the statutory predecessor of § 902, the Supreme Court said:

> "If, as is admitted, the purpose is to avoid double taxation, the statute, as written, accomplishes that result. The parent receives dividends. Such dividends, not its subsidiary's profits, constitute its income to be returned for [United States] taxation." *American Chicle Co.* v. *United States, supra,* 316 U.S. 450, 452.

By limiting its credit to the standard tax appropriate to the dividend, Article XIII(1) does not permit any credit for standard tax which is not allocable to earnings distributed as dividends.[11] Section 902 allows a credit only for foreign taxes on the portion of the foreign corporation's earnings which are distributed as dividends to a domestic corporation.

---

[10] Alexander, The Income Tax Convention with the United Kingdom, 2 Tax L. Rev. 295.

[11] After *Biddle* the only shareholder entitled to a tax credit for United Kingdom standard tax was a corporate shareholder qualifying for indirect credit under the predecessor of § 902. Although Article XIII(1) is available to domestic corporations, it is clear that this provision was undertaken in order to give relief from *Biddle* to individual shareholders and to domestic corporations which did not own enough stock to qualify for § 902 treatment. Senate Hearings before a Subcommittee of the Committee on Foreign Relations on Conventions with Great Britain and Ireland Respecting Income and Estate Taxes, 79th Cong., 1st Sess., p. 47 (2 Leg. Hist. of Tax Conv., 2583, 2613).

Having availed itself of the Article XIII(1) credit for the standard tax appropriate to the dividend, the taxpayer's use of a § 902 credit for the remaining standard tax results in a credit for foreign taxes allocable to earnings which were not distributed as dividends.[12] A domestic corporation is not taxed on the entire earnings of a foreign corporation in which it owns stock unless the foreign corporation distributes all of its earnings as dividends to the domestic corporation. In the present case the two foreign subsidiaries retained a portion of their earnings. Because the United States taxes only the dividends paid by foreign corporations, there is no danger of international double taxation with respect to the earnings which the foreign corporation retains. In order to effectuate the purpose of the Code and the Convention, the taxpayer must elect either Article XIII(1) or § 902 of the Internal Revenue Code for computing its foreign tax credit with respect to the United Kingdom standard tax appropriate to the dividend.[13]

CONCLUSION

We conclude that the District Court erred in ordering a refund of taxes based upon the taxpayer's use of Article XIII(1) of the Convention and § 902 of the Code in combination. To allow resort to both the Convention and the statute would be to permit credits for standard taxes in

---

[12] The Government concedes the correctness of the taxpayer's computation to the extent that § 902 is used to compute credits for the United Kingdom profits tax and the miscellaneous foreign income taxes.

[13] Ordinarily § 902 provides a greater tax benefit than Article XIII(1), but under certain circumstances the Article XIII(1) credit may be more favorable. E.g., when the standard tax rate has increased between the time the British subsidiary earns the income and pays the standard tax and the time that it distributes a portion of its accumulated income as a dividend. This is true because § 902 credit is based on the tax rate applicable at the time the subsidiary pays the standard tax, but Article XIII(1) credit is based on the tax rate applicable at the time the dividend is paid.

excess of that which Congress, in enacting § 902, deemed necessary to alleviate the burden of international double taxation.

As said by this Court speaking through Judge Simons in *Gentsch* v. *Goodyear Tire & Rubber Co.*, 151 F.2d 997, 1000:

> "We think, therefore, that the controlling principle of statutory construction is not that which requires special tax exemptions to be strictly construed, but rather the principle so often announced as not to require citation, that statutes must be so construed as to give effect of their general purpose and to implement the policy of the Congress. Relief from double taxation is not so much an act of grace as one of justice in determining the true net income of the taxpayer."

We hold that § 902 affords no credit for standard taxes in combination with Article XIII(1) and that the statute and convention are mutually exclusive. "Our interpretation affords every benefit negotiated for by the parties to the Convention on behalf of their respective residents and prevents an unintended tax windfall . . ." to the taxpayers in the present case. *Maximov* v. *United States*, 373 U.S. 49, 56.

The judgment of the District Court is reversed and the case remanded for further proceedings not inconsistent with this opinion.

APPENDIX B

UNITED STITES COURT OF APPEALS FOR THE SIXTH CIRCUIT

NATIONAL CASH REGISTER COMPANY,
Plaintiff-Appellee,

v.

UNITED STATES OF AMERICA, *Defendant-Appellant.*

Order

Before O'SULLIVAN and PHILLIPS, Circuit Judges, and CECIL, Senior Circuit Judge.

Upon consideration, it is ORDERED that the petition for rehearing, for withdrawal of the opinion of this Court dated September 12, 1968, and for either affirmance or scheduling for reargument, be and hereby is overruled.

Entered by order of the Court.

Filed: October 23, 1968

IN THE

Supreme Court of the United States

OCTOBER TERM, 1968

No. 955

THE NATIONAL CASH REGISTER COMPANY, *Petitioner*,

v.

UNITED STATES OF AMERICA

APPENDIX C
TO PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

PHILIP R. BROOKS
COWDEN, PFARRER, CREW & BROOKS
Winters Bank Building
Dayton, Ohio 45402

CHARLES E. MARTIN
JAMES E. RAMBO
Main and K Streets
Dayton, Ohio 45409

JOSEPH G. BLAIR
J. RUSSELL PEARSON
GEORGE W. BEATTY
[illegible]
[illegible]
[illegible]

INDEX

	Page
Docket Entries	1a
Complaint	3a
Defendant's Answer	9a
Stipulation	10a
Order Submitting Case	12a
Findings of Fact, Discussion and Conclusions of Law, and Order of District Court	13a
Judgment of District Court	33a
Order Amending Findings of Fact	34a
Notice of Appeal	35a

UNITED STATES DISTRICT COURT

Southern District of Ohio
Western Division

Civil Action No. 3188 (At Dayton, Ohio)

THE NATIONAL CASH REGISTER CO.,
Plaintiff,

v.

UNITED STATES OF AMERICA,
Defendant.

DOCKET ENTRIES

Date	Proceeding
6-8-65	Complaint filed.
	Summons issued with copies of complaint to U. S. Marshal for service.
6-16-65	Summons returned, executed & filed. Marshal's fee $3.00.
8-9-65	Defendant's Answer, filed.
	Defendant's Interrogatories, filed.
9-7-65	Motion to extend Plaintiff's time, filed.
9-15-65	Plaintiffs answer to defendants interrogatories filed.
9-15-65	Plaintiff's time extended to Sept. 17, 1965 to file answer, filed.
6-6-66	Stipulation filed
	ORDER: Plaintiff's brief to be filed on or before July 1, 1966 and Defdt's. brief on or before September 1, 1966, filed.
6-27-66	Plaintiff's Brief, filed.
8-12-66	Defendant's Brief filed.

Docket Entries

9-28-66	Reply brief for Plaintiff filed.
10-19-66	Defendants reply brief filed.
4-7-67	Findings of Fact, Discussion & Conclusions of Law & Order, filed. Judgment Entry to come.
5-11-67	Order amending findings of Fact, filed. Judgment in favor of the plaintiff and against the defendant in the amount of $508,643.65 tax and $96,-263.84 assessed interest with 6% according to law, filed.
7-10-67	NOTICE OF APPEAL FILED.
7-20-67	Transcript of Proceedings, filed.

(CAPTION OMITTED)

COMPLAINT

(Filed June 8, 1965)

Count One

(1) This action is instituted against defendant pursuant to the provisions of section 1346(a)(1) of Title 28 of the United States Code for the recovery of income taxes erroneously assessed and collected from plaintiff for the calendar year 1958.

(2) Plaintiff at all times material herein was, and is, a Maryland corporation, with its principal place of business in Dayton, Ohio. Plaintiff employs the accrual method of accounting and maintains its books of account and files its tax returns on the basis of the calendar year.

(3) At all times during the year 1958 plaintiff was the owner of all the voting stock of The National Cash Register Company Limited and of The National Cash Register Company (Manufacturing) Limited, corporations of limited liability, organized under the laws of, and residents of, the United Kingdom of Great Britain and Northern Ireland (hereinafter called the "United Kingdom"). During 1958 these corporations (hereinafter sometimes called the "United Kingdom subsidiaries") had net earnings, computed before payment of the taxes described in paragraph (4) below, of the following amounts:

	Net Earnings
The National Cash Register Company Limited	$2,409,564.52
The National Cash Register Company (Manufacturing) Limited	3,927,833.75

During 1958 the United Kingdom subsidiaries paid to plaintiff, out of the aforesaid net earnings, dividends in the following amounts:

	Dividends Paid
The National Cash Register Company Limited	$1,019,190.01
The National Cash Register Company (Manufacturing) Limited	1,571,981.25

(4) Each of plaintiff's United Kingdom subsidiaries was subject to the United Kingdom income tax (hereinafter referred to as the "Standard Tax") and the United Kingdom profits tax. For the year 1958 plaintiff's United Kingdom subsidiaries paid the following United Kingdom taxes:

	Standard Tax	Profits Tax	Miscellaneous Income Taxes
The National Cash Register Company Limited	$ 961,654.96	$207,583.57	$5,081.06
The National Cash Register Company (Manufacturing) Limited	1,705,578.99	335,393.10	None

Receipts evidencing the payment of all of the aforesaid taxes by plaintiff's United Kingdom subsidiaries have been delivered to examining agents of the Internal Revenue Service.

(5) The amount of Standard Tax appropriate to the dividends paid to plaintiff by each of the United Kingdom subsidiaries as set forth in paragraph (3) of this complaint was as follows:

Standard Tax appropriate to dividends paid by The National Cash Register Company Limited	$644,793.67
Standard Tax appropriate to dividends paid by The National Cash Register Company (Manufacturing) Limited	994,518.75

(6) In its tax return for the year 1958 and upon audit thereof by the Internal Revenue Service, plaintiff claimed the relief provided by Article XIII(1) of the Income Tax Convention between the United States and the United Kingdom (hereinafter referred to as the "Convention") with respect to the dividends paid to plaintiff by its United Kingdom subsidiaries as set forth in paragraph (3) above. Pursuant to the Convention, plaintiff elected to include in its gross income the Standard Tax appropriate to such dividends as set forth in paragraph (5) above, and claimed such Standard Tax as a direct credit under section 901 of the Internal Revenue Code of 1954, as amended (hereinafter called the "Code").

(7) In addition thereto, plaintiff claimed it was entitled to an indirect credit for taxes deemed to have been paid under Section 902 of the Code, based upon the United Kingdom taxes described in paragraph (4) above reduced by the Standard Tax actually claimed as a direct credit under the Convention and section 901 of the Code.

(8) As so claimed, plaintiff's foreign tax credits under the Convention and sections 901-904 of the Code with respect to its United Kingdom subsidiaries are as follows:

	Direct Credit Under Convention & Sec. 901	Indirect Credit for Taxes Deemed Paid Under Sec. 902	Total
The National Cash Register Company Limited	$644,793.67	$365,677.07	$1,010,470.74
The National Cash Register Company (Manufacturing) Limited	994,518.75	669,636.02	1,664,154.77
Total			$2,674,625.51

(9) Upon the final audit of plaintiff's 1958 tax return the Internal Revenue Service erroneously refused to allow plaintiff's foreign tax credits as computed above and maintained that if a direct credit is claimed under the Convention and section 901 of the Code, the United Kingdom taxes available for the indirect credit under section 902 of the Code must exclude all of the Standard Taxes paid by plaintiff's United Kingdom subsidiaries, and not just the portion thereof appropriate to the dividends paid by such subsidiaries. The Internal Revenue Service proceeded to compute plaintiff's foreign tax credits for United Kingdom taxes solely under section 902 of the Code and asserted a deficiency, adjusted by other items, in the amount of $444,133.54 which was paid by plaintiff on or about December 28, 1962, together with interest thereon.

(10) Within the time or times prescribed by law plaintiff on December 26, 1963 filed with the Internal Revenue Service

its claim for refund of a portion of its income taxes for the year 1958 with deficiency interest and interest on both amounts as provided by law. Said claim was based upon the grounds that plaintiff was entitled to foreign tax credits for United Kingdom taxes computed as set forth in paragraphs (6), (7) and (8) above. The amount of tax for which refund was claimed on these grounds was $508,643.65. Said claim was erroneously disallowed on May 4, 1964.

Count Two

(11) Plaintiff realleges the allegations of paragraphs (1) through (9) of Count One above, and alleges in the alternative that in any event it is entitled to—

(a) a direct foreign tax credit under the Convention and section 901 of the Code as set forth in paragraph (8) of Count One above, plus

(b) an indirect credit for taxes deemed to have been paid under section 902 of the Code, based upon the United Kingdom taxes described in paragraph (4) of Count One reduced by the amount of Standard Tax which would have been allowable as a direct credit under the Convention and section 901 of the Code had the entire 1958 after-tax earnings of plaintiff's two United Kingdom subsidiaries been distributed as dividends to plaintiff.

(12) In its claim for refund referred to in paragraph (10) of Count One, plaintiff raised this alternative ground for refund and such alternative ground was also erroneously disallowed by the Internal Revenue Service on May 4, 1964.

WHEREFORE, plaintiff demands judgment against defendant in the amount of $508,643.65, or such other amount to which it may be legally entitled, together with appropriate

deficiency interest and with statutory interest on both amounts as provided by law.

/s/ Philip R. Becker
PHILIP R. BECKER
Cowden, Pfarrer, Crew & Becker
712 Winters Bank Building
Dayton, Ohio 45402

/s/ Joseph G. Blandi
JOSEPH G. BLANDI

/s/ John P. Lipscomb
JOHN P. LIPSCOMB

/s/ George W. Beatty
GEORGE W. BEATTY
Lee, Toomey & Kent
1200 18th Street, N.W.
Washington, D.C. 20036

Attorneys for Plaintiff

(CAPTION OMITTED)

DEFENDANT'S ANSWER

(Filed August 9, 1965)

The United States of America by its attorney, Joseph P. Kinneary, United States Attorney for the Southern District of Ohio, states in answer to the allegations of the plaintiff's complaint that:

Count One

1. It admits the allegations of paragraph 1, except that it denies that any tax was erroneously assessed or collected from the plaintiff.

2. It admits the allegations of paragraph 2.

3. It admits the allegations of paragraph 3.

4. It presently is without knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 4.

5. It admits the allegations of paragraph 5.

6. It admits the allegations of paragraph 6.

7. It admits the allegations of paragraph 7.

8. It presently is without knowledge or information sufficient to form a belief as to the truth of the allegations of paragraph 8.

9. It admits the allegations of paragraph 9, except that it denies that the determinations of the Internal Revenue Service were erroneous.

10. It admits the allegations of paragraph 10, except that it denies that the disallowance of the plaintiff's claim was erroneous.

Count Two

11. It denies the allegations of paragraph 11, except that it admits the allegations of paragraphs 1 through 9 of Count One, realleged by paragraph 11, to the same extent that it admits those allegations in its answer to Count One.

12. It admits the allegations of paragraph 12, except that it denies that the disallowance by the Internal Revenue Service was erroneous.

WHEREFORE, the defendant demands judgment dismissing the plaintiff's complaint with costs to be paid to it by the plaintiff.

/s/ Joseph P. Kinneary
United States Attorney

(CAPTION OMITTED)

STIPULATION

(Filed June 6, 1966)

The parties hereby stipulate that the statements in paragraphs 1-18 shall be taken as true for the purposes of this action; and the parties further agree as provided in paragraphs 19 and 20.

* * *

[For paragraphs 1-18, see paragraphs 1-18 of the Findings of Fact, *infra.*]

* * *

19. The plaintiff's claim for relief in this action is submitted to the Court for judgment on the plaintiff's complaint, the defendant's answer, and the preceding paragraphs of this stipulation, without the introduction of other evidence by either party.

Stipulation

20. Unless the Court expressly orders otherwise, if the Court determines that the plaintiff is entitled to any relief against the defendant on its complaint, the parties will jointly compute the amount of the judgment in accordance with the Court's findings of fact and conclusions of law, and submit the computation to the Court for its approval and the entry of a judgment; if the parties cannot agree on the proper computation, the Court will determine the amount of the judgment; and until such time, no final judgment shall be deemed to have been entered in this action.

/s/ Philip R. Becker
Philip R. Becker
Cowden, Pfarrer, Crew & Becker
712 Winters Bank Building
Dayton, Ohio 45402

/s/ George W. Beatty
George W. Beatty
Lee, Toomey & Kent
1200 18th Street, N.W.
Washington, D.C. 20036
Attorneys for Plaintiff

/s/ Donald R. Anderson
Donald R. Anderson

/s/ Burton G. Lipsky
Burton G. Lipsky
Trial Attorneys
Department of Justice
Washington, D.C. 20530
Attorneys for Defendant

(CAPTION OMITTED)

ORDER

(Filed June 6, 1966)

By agreement of counsel for both parties, it is ORDERED that this cause be submitted to the Court, pursuant to the stipulation heretofore filed herein, on the briefs of counsel and on oral argument. It is ORDERED further that Plaintiff's brief be filed on or before July 1, 1966, Defendant's brief on or before September 1, 1966 and Plaintiff's reply brief on or before October 1, 1966. Thereafter the cause will be assigned by the Court for oral argument.

/s/ Carl A. Weinman
Judge

/s/ Philip R. Becker
Philip R. Becker
Cowden, Pfarrer, Crew & Becker
Counsel for Plaintiff

/s/ Roger J. Makley
Roger J. Makley
Asistant United States Attorney
Counsel for Defendant

(CAPTION OMITTED)

FINDINGS OF FACT, DISCUSSION AND CONCLUSIONS OF LAW, ORDER

(Entered April 7, 1967)

The parties to this action have agreed to submit plaintiff's claim for relief to the Court for judgment on plaintiff's complaint, defendant's answer and a stipulation filed June 6, 1966. That stipulation is now adopted by the Court as its findings of fact.

FINDINGS OF FACT

1. The plaintiff at all times material to this action was, and is, a Maryland corporation, with its principal place of business in Dayton, Ohio. The plaintiff employs the accrual method of accounting and maintains its books of account and files its tax returns on the basis of the calendar year.

2. The plaintiff timely filed its U. S. Corporation Income Tax Return for its calendar year 1958 with the District Director of Internal Revenue at Cincinnati, Ohio, on June 15, 1959. On its return plaintiff reported and [*sic*] income tax liability for 1958 of $11,337,786.67, of which $7,825,000 had been previously paid to the defendant and of which the balance of $3,512,786.67 was paid to the defendant with the return. On February 10, 1961 the Internal Revenue Service timely assessed against the plaintiff a deficiency of such tax of $855,753.38 and interest thereon of $83,667.22, which deficiency and interest was satisfied by a credit of $61,574.26 allowed to the plaintiff by the defendant on February 15, 1961 and a payment of $877,846.34 by the plaintiff to the defendant on February 24, 1961. On January 11, 1963, the Internal Revenue Service timely assessed

against the plaintiff a further deficiency of such tax of $444,-133.54 and interest thereon of $100,876.05, which deficiency and interest of $545,009.59 was paid by the plaintiff to the defendant on December 28, 1962. On May 7, 1964, the defendant refunded to the plaintiff $84,410.73 of the tax and $19,172.20 of the interest which had been assessed against it, and the defendant paid to the plaintiff interest of $8,337.72 on the amount refunded.

3. On December 26, 1963, the plaintiff timely (with respect to all tax and interest paid by the plaintiff for 1958) filed with the Internal Revenue Service a claim for refund of tax and interest paid by it for 1958. On May 4, 1964, the District Director notified the plaintiff by certified mail that its claim with respect to the issue in this action had been disallowed. No part of the refund of tax or interest to which the plaintiff would be entitled upon the allowance of its claim with respect to the issue in this action has been paid or credited to the plaintiff by the defendant. Ex. A is a true copy of the claim for refund filed by the plaintiff; but no statement contained in the claim is stipulated to by the parties unless the statement is expressly stipulated to elsewhere in this Stipulation, and the portion of the claim entitled "Claim with respect to Unused Foreign Tax Credit Carrybacks from 1959 and 1960 for Taxes Paid to Certain Other Foreign Countries" has been allowed and is not in issue in this action.

4. At all times during the year 1958 the plaintiff owned all of the voting stock of The National Cash Register Company Limited ("NCR Ltd.") and of The National Cash Register (Manufacturing) Limited ("NCR Mfg."), corporations of limited liability, organized under the laws of, and residents of, the United Kingdom of Great Britain and Northern Ireland ("United Kingdom"). During 1958 these corporations (the plaintiff's United Kingdom subsidiaries") had "total profits" (before payment of the taxes stated in paragraph 5, *infra*) and

"accumulated profits" (total profits less such taxes), in the following amounts:

	"Total Profits"	"Accumulated Profits"
NCR Ltd.	$2,409,564.52	$1,235,244.93
NCR Mfg.	3,927,833.75	1,886,861.66
	$6,337,398.27	$3,122,106.59

The amount stated as accumulated profits constituted the subsidiary's "accumulated profits" for 1958 as defined by Section 902(c)(1) of the Internal Revenue Code of 1954 as enacted prior to its amendment in 1960.

5. For the year 1958 the plaintiff's United Kingdom subsidiaries paid the following taxes:

	UNITED Kingdom Standard Tax	United Kingdom Profits Tax	Miscellaneous Foreign Income Taxes	Total Tax
NCR Ltd.	$ 961,654.96	$207,583.57	$5,081.06	$1,174,319.59
NCR Mfg.	1,705,578.99	335,393.10	- - -	2,040,972.09
	$2,667,233.95	$542,976.67	$5,081.06	$3,215,291.68

All of the above taxes constitute "income, war profits, or excess profits taxes" within the meaning of that phrase as used in Sections 901 through 905 of the Internal Revenue Code of 1954. Except for the "Miscellaneous Foreign Income Taxes," all of the above taxes constitute "United Kingdom tax" within the meaning of Article I of the Income Tax Convention of April 16, 1945, between the United States and the United Kingdom (the "Convention"), as amended by the Supplementary Protocol of August 19, 1957; and the above taxes were the only such taxes paid or accrued in 1958 by the plaintiff's United Kingdom subsidiaries. The United Kingdom Standard Tax

and United Kingdom Profits Tax were paid by the plaintiff's United Kingdom subsidiaries to the United Kingdom; the "Miscellaneous Foreign Income Taxes" were paid by NCR Ltd. to countries other than the United Kingdom (or the United States), but for the purposes of Section 904 of the Internal Revenue Code of 1954 are deemed to have been paid to the United Kingdom as the country in which NCR Ltd. was incorporated.

6. For the United Kingdom tax year beginning April 6, 1958, the plaintiff's United Kingdom subsidiaries were subject to the United Kingdom income tax and the United Kingdom profits tax. The income tax consisted of a "standard tax" imposed at a flat rate of 38.75% on corporations and individuals and a "surtax" imposed at graduated rates on individuals only. The profits tax was imposed on corporations only at the rate of 10%. Both the standard tax and the profits tax were imposed on a resident corporation's net earnings for the taxable year without deduction of any dividend declared from those earnings; and neither tax was deductible in computing the other.

7. A corporation resident in the United Kingdom could declare dividends in 1958 either "with deduction of standard tax" or "free of standard tax". When a dividend was declared "with deduction of standard tax", the corporation computed the standard tax payable on the declared amount of the dividend at the standard tax rate in effect, when the dividend was declared (even though this rate may have been different than the standard tax rate in effect when the corporation earned the profits being distributed), deducted the computed amount from the declared amount of the dividend, and paid the balance of the declared amount to the shareholder. When a dividend was declared "free of standard tax", the declared amount of the dividend was paid to the shareholder.

8. During 1958 the amount of a dividend received from a United Kingdom corporation could be "grossed up" to an

amount which, after deduction from that "grossed up" amount of the standard tax payable on that "grossed up" amount, equaled the amount of the dividend received. The standard tax payable on the "grossed up" amount was known as the standard tax "appropriate to" the dividend received. (Mathematically, the "grossed up" amount equaled the dividend received divided by the percentage by which the applicable rate of the standard tax was less than 100%; the standard tax "appropriate to" the dividend received was the "grossed up" amount less the dividend received. If the dividend received was *d*, and the rate of the standard tax was *r*, the "grossed up" amount of *d* was $\frac{d}{1-r}$.) When a dividend was declared "with deduction of standard tax", the standard tax "appropriate to" the dividend received by the shareholder was the amount by which the dividend declared exceeded the dividend received by the shareholder; and the dividend declared was the "grossed up" amount of the dividend received. When a dividend was declared "free of standard tax", the standard tax "appropriate to" the dividend was the amount by which the "grossed up" amount of the dividend declared exceeded the dividend declared. The standard tax "appropriate to" a dividend, as described in this paragraph, constituted "the United Kingdom tax appropriate to such dividend" as that phrase was used in paragraph (1) of Article XIII of the Convention, as amended by the Supplementary Protocol of August 19, 1957.

9. During 1958 a shareholder of a United Kingdom corporation was not subject to the assessment of any standard tax on the amount of a dividend received from the corporation, but was subject (in the case of an individual) to the assessment of a surtax on that amount. For United Kingdom tax purposes other than the assessment of the standard tax, the shareholder included in his income the declared amount of a

dividend paid "with deduction of standard tax" and the declared amount "grossed up" of a dividend paid "free of standard tax"; thus, in both cases, the shareholder included in his income the amount which he received from the corporation and the standard tax "appropriate to" that amount.

10. The dividends received by the plaintiff from its United Kingdom subsidiaries in 1958 were declared "free of standard tax". The amount of the dividends declared and received by the plaintiff, their "grossed up" amount, and the standard tax "appropriate to" the dividends were:

	DIVIDEND Declared and Received	"Grossed Up" Amount	Standard Tax "Appropriate to" Dividend
NCR Ltd.	$1,019,190.01	$1,663,983.68	$ 644,793.67
NCR Mfg.	1,571,981.25	2,566,500.00	994,518.75
	$2,591,171.26	$4,230,483.68	$1,639,312.42

The above dividends were received by the plaintiff from sources within the United Kingdom and were includible in the plaintiff's United States taxable income for 1958. The plaintiff received in 1958 from NCR Mfg. other income of $1,693,-857.13 from sources within the United Kingdom which was also includible in the plaintiff's United States taxable income for 1958.

11. If the "accumulated profits" for 1958 of the plaintiff's United Kingdom subsidiaries (stated in par. 4, *supra*) were "grossed up" as if they had been entirely distributed as dividends declared "free of standard tax", their "grossed up" amounts and the standard tax "appropriate to" the accumulated profits would have been:

	"Accumulated Profits"	"Grossed Up" Amount	Standard Tax "Appropriate to" Accumulated Profits
NCR Ltd.	$1,235,244.93	$2,016,726.40	$ 781,481.48
NCR Mfg.	1,886,861.66	3,080,590.47	1,193,728.80

12, The Cumulative Bulletin, published by the Internal Revenue Service, contains true and complete texts of the Convention, and the Supplementary Protocols thereto, as follows:

Convention of April 16, 1945	1947-1 Cum. Bull. 209
Supplementary Protocol of June 6, 1946	1947-1 Cum. Bull. 217
Supplementary Protocol of May 25, 1954.	1957-1 Cum. Bull. 665
Supplementary Protocol of August 19, 1957	1958-2 Cum. Bull. 1078

Article I of the Convention (1947-1 Cum. Bull. 209) provided in 1958 that:

> "(1) The taxes which are the subject of the present convention are:
>
> (a) In the United States of America: The Federal income taxes, including surtaxes and excess profits taxes (hereinafter referred to as United States tax).
>
> (b) In the United Kingdom of Great Britain and Northern Ireland: The income tax (including surtax), the excess profits tax and the national defense contribution (hereinafter referred to as United Kingdom tax).

(2) The present convention shall also apply to any other taxes of a substantially similar character imposed by either contracting party subsequently to the date of signature of the present convention * * *"

Article XIII of the Convention, as amended (1958-2 Cum. Bull. 1081), provided in 1958 that:

"(1) Subject to Sections 901 to 905 of the United States Internal Revenue Code as in effect on the 1st day of January 1956, United Kingdom tax shall be allowed as a credit against United States tax. For this purpose (a) the recipient of a dividend paid by a corporation which is a resident of the United Kingdom shall be deemed to have paid the United Kingdom tax appropriate to such dividend * * * if the recipient of the dividend * * * elects to include in his gross income for the purposes of United States tax the amount of such United Kingdom income tax."

13. In 1956 the Internal Revenue Service published Revenue Ruling 56-239, the complete text (1956-1 Cum. Bull. 321) of which is:

"Advice has been requested whether a domestic corporation which owned a majority of the stock of a British corporation, including at least 10 percent of the voting stock of such corporation, is entitled to either a deduction under section 164 of the Internal Revenue Code of 1954, or a credit under section 901, for the standard tax appropriate to such dividends paid by the British corporation.

The principal question presented is whether the decision in *Mary D. Biddle et al.* v. *Commissioner,* 302 U.S. 573, Ct. D. 1303, C.B. 1938-1, 309, or article XIII (1) of the income tax convention between the United States and the United Kingdom, Treasury Decision 5569, C.B. 1947-2, 100 is applicable with respect to the standard tax

on dividends received by a domestic corporation from a British corporation.

The Biddle decision determined that the British standard tax paid by a British corporation is laid not upon the shareholder but upon the British corporation. Accordingly, it was held that although the tax burden of the corporation is passed on to its shareholders, the United States statutes do not take that fact into consideration in ascertaining the tax obligation of the shareholder. These statutes do not treat as taxpayers those upon whom no legal duty to pay the tax is laid. Therefore, on the basis of the Biddle decision, no deduction is allowable to the shareholder under section 23(c)(1)(C) of the Internal Revenue Code of 1939 (now section 164(b)(6) of the Internal Revenue Code of 1954) and no credit is allowable to the shareholder under section 131(a) of the 1939 Code (now section 901(a) of the 1954 Code) for British standard tax paid by corporations.

Under article XIII(1) of the United States — United Kingdom income tax convention, if the shareholder should elect to include in his gross income the amount of the standard tax appropriate to the dividend paid by the British corporation, the shareholder shall be deemed to have paid such tax. Consequently, under the convention, a credit would be allowable to the shareholder under section 901 of the Code for such tax paid. See Rev. Rul. 54-533, C.B. 1954-2, 210. If additional United Kingdom income, war profits, or excess profits taxes not covered by the convention are paid by the British corporation, an additional credit based on such other taxes is allowable to the domestic corporation under section 902, because the domestic corporation owns at least 10 percent of the voting stock of the British corporation.

If the domestic corporation should not elect to treat the standard tax in accordance with article XIII(1) of the convention, the provisions of section 902 would be applicable to both the standard tax and other income, war profits and excess profits taxes paid by the British cor-

poration. Under this section, such taxes would not be included in the shareholder's gross income, but, in accordance with section 902 of the Code, a portion of the taxes paid by the British subsidiary would be deemed to have been paid by the domestic corporation.

Article XIII(1) of the convention with the United Kingdom has no application to the allowance of a deduction to a shareholder for the standard tax paid by a British corporation. Therefore, as held in the Biddle case, the shareholder may not claim a deduction for such tax paid by the corporation."

14. In its 1958 United States income tax return the plaintiff included in its taxable income the amount of $4,230,483.69 consisting of the dividends received from its United Kingdom subsidiaries and the standard tax "appropriate to" such dividends, which together equaled the "grossed up" amounts stated in par. 10, *supra*. Against the income tax otherwise payable on its taxable income the plaintiff claimed a credit under Section 901 of the Internal Revenue Code of 1954 in the amount of $2,674,625.51 with respect to the taxes (stated in par. 5, *supra*) which had been paid by its United Kingdom subsidiaries. The amount of the credit was determined by the plaintiff as follows:

(a) Under Article XIII(1) of the Convention, a "direct credit" in the amount of $1,639,312.42 equal to the total standard tax "appropriate to" the dividends which the plaintiff received from its United Kingdom subsidiaries (as stated in par. 10,*supra*), and

(b) "Indirect credits" in the total amount of $1,035,313.09 computed under Section 902 separately for the taxes paid by each of its United Kingdom subsidiaries according to the following formula:

$$\frac{\text{"grossed up" amount of dividend}}{\text{subsidiary's "accumulated profits"}} \times \frac{\text{subsidiary's "accumulated profits"}}{\text{subsidiary's "total profits"}} \times \text{taxes paid by the subsidiary less the standard tax "appropriate to" the dividend}$$

The actual computation of the "indirect credit" for the taxes paid by NCR Ltd. was:

$$\frac{\$1,663,983.68^{1}}{\$1,235,244.93^{2}} \times \frac{\$1,235,244.93^{2}}{\$2,409,564.52^{2}} \times (\$1,174,319.59^{3} - \$644,793.67)^{1} = \$365,677.07$$

The actual computation of the "indirect credit" for the taxes paid by NCR Mfg. was:

$$\frac{\$2,566,500.00^{1}}{\$1,886,861.66^{2}} \times \frac{\$1,886,861.66^{2}}{\$3,927,833.75^{2}} \times (\$2,019,345.93^{4} - \$994,518.75)^{1} = \$669,636.02$$

[1] Par. 10, *supra*.
[2] Par. 4, supra.
[3] Par. 5, *supra*.
[4] Of the total of $2,040,972.09 taxes paid by NCR Mfg. (Par. 5, *supra*), $21,626.16 was treated as having been paid in 1959, leaving a balance of $2,019,345.93.

15. If the plaintiff was not entitled to a credit in the amount of $2,674,625.51 as computed in the preceding paragraph, it claims (alternatively) a credit under Section 901 of the Internal Revenue Code of 1954 in the amount of $2,450,065.84 computed as follows:

Findings of Fact

(a) Under Article XIII(1) of the Convention, a "direct credit' 'in the amount of $1,639,312.42 equal to the total standard tax "appropriate to" the dividends which the plaintiff received from its United Kingdom subsidiaries (as stated in par. 10, *supra*); and

(b) "Indirect credits" in the total amount of $810,753.42 computed under Section 902 separately for the taxes paid by each of its United Kingdom subsidiaries according to the following formula:

$$\frac{\text{"grossed up" amount of dividend}}{\text{subsidiary's "accumulated profits"}} \times \frac{\text{subsidiary's "accumulated profits"}}{\text{subsidiary's "total profits"}} \times \text{taxes paid by the subsidiary less standard tax "appropriate to" amount of its "accumulated profits"}$$

The actual computation of the "indirect credit" for the taxes paid by NCR Ltd. would be:

$$\frac{\$1,663,983.68^{1}}{\$1,235,244.93^{2}} \times \frac{\$1,235,244.93^{2}}{\$2,409,564.52^{2}} \times (\$1,174,319.59^{3} - \$781,481.48)^{4} = \$271,283.96$$

The actual computation of the "indirect credit" for the taxes paid by NCR Mfg. would be:

$$\frac{\$2,566,500.00^{1}}{\$1,886,861.66^{2}} \times \frac{\$1,886,861.66^{2}}{\$3,927,833.75^{2}} \times (\$2,019,345.93^{5} - \$1,193,728.80)^{4} = \$539,469.46$$

1 Par. 10, *supra*.
2 Par. 4, *supra*.
3 Par. 5, *supra*.

[4] Par. 11, *supra*.

[5] Of the total of $2,040,972.09 taxes paid by NCR Mfg. (par. 5, *supra*), $21,626.16 was treated as having been paid in 1959, leaving a balance of $2,019,345.93.

16. Upon its audit of the plaintiff's income tax return for 1958, the Internal Revenue Service adjusted the plaintiff's taxable income; and, against the income tax otherwise payable on the plaintiff's taxable income (as adjusted by the Internal Revenue Service), the Internal Revenue Service allowed a credit under Section 901 in the amount of $1,313,539.40 with respect to the taxes which had been paid by the plaintiff's United Kingdom subsidiaries. The Internal Revenue Service disallowed the greater credit claimed by the plaintiff (par. 14, *supra*) and assessed against the plaintiff a deficiency of income tax (par. 2, *supra*). The Internal Revenue Service reduced the plaintiff's taxable income (as reported) by the amounts (stated in par. 10, *supra*) of the standard tax "appropriate to" the dividends which the plaintiff received from its United Kingdom subsidiaries, so that the plaintiff's taxable income included only the amounts of the dividends declared and received (as stated in par. 10); and the Internal Revenue Service did not allow any "direct credit" under the Convention. The credit which the Internal Revenue Service allowed was the total of "indirect credits" computed under Section 902 separately for the taxes paid by each of the plaintiff's United Kingdom subsidiaries according to the following formula:

$$\frac{\text{dividend received by plaintiff}}{\text{subsidiary's "accumulated profits"}} \times \frac{\text{subsidiary's "accumulated profits"}}{\text{subsidiary's "total profits"}} \times \text{Total taxes paid by subsidiary}$$

The actual computation of the "indirect credit" for the taxes paid by NCR Ltd. was:

$$\frac{\$1{,}019{,}190.01^{1}}{\$1{,}235{,}244.92^{2}} \times \frac{\$1{,}235{,}244.93^{2}}{\$2{,}409{,}564.52^{2}} \times \$1{,}174{,}319.59^{3} = \$496{,}710.05$$

The actual computation of the "indirect credit" for the taxes paid by NCR Mfg. was:

$$\frac{\$1{,}571{,}981.25^{1}}{\$1{,}886{,}861.66^{2}} \times \frac{\$1{,}886{,}861.66^{2}}{\$3{,}927{,}833.75^{2}} \times \$2{,}040{,}972.11^{3} = \$816{,}829.35$$

[1] Par. 10, *supra*.
[2] Par. 4, *supra*.
[3] Par. 5, *supra*.

17.* The credit under Section 901 computed by the Internal Revenue Service as stated in the preceding paragraph resulted in a larger credit (and a smaller tax liability) for the plaintiff for 1958 than if the Internal Revenue Service had included in the plaintiff's taxable income the standard tax "appropriate to" the dividends received by the plaintiff from its United Kingdom subsidiaries, allowed a "direct credit" in the amount of such standard tax under the Convention, and allowed "indirect credits" computed under Section 902 using the formula stated in the preceding paragraph modified by substituting (a) the "'grossed up' amount of the dividend" for "dividend received by plaintiff" and (b) the "taxes other than standard tax paid by subsidiary" for "total taxes paid by subsidiary".

* The text of this paragraph has been amended. See Order Amending Findings of Fact, *infra*.

Findings of Fact

18. The credits under Section 901 claimed by the plaintiff either as in par. 14, *supra,* or as in par. 15, *supra,* and the credit allowed by the Internal Revenue Service as in par. 16, *supra,* are less than the same proportion of the tax against which the credit would be taken which the plaintiff's taxable income from sources within the United Kingdom for the year 1958 bore to its entire taxable income for the year 1958 as required by Section 904 of the Internal Revenue Code of 1954 prior to its amendment in 1960.

Question Presented: May a United States corporate taxpayer which received dividends from its wholly owned United Kingdom subsidiaries and elects, under the United States-United Kingdom Income Tax Convention of 1945, as amended by the Supplementary Protocol of August 19, 1957, (hereinafter referred to as the "Convention") and Section 901, Internal Revenue Code of 1954, to claim a direct foreign tax credit for the United Kingdom standard tax "appropriate to" those dividends also claim an indirect foreign tax credit under Section 902, Internal Revenue Code, for the remaining portion of the United Kingdom standard tax paid by the United Kingdom subsidiaries.

The plaintiff's contentions are 1) that under Article XIII (1) of the Convention, plaintiff had the option of treating the standard tax "appropriate to" the dividends plaintiff received as a withholding tax for which a direct credit could be taken, provided plaintiff included the amount of that tax in income, 2) that, in addition to the aforementioned direct credit, plaintiff is entitled to an indirect credit under Section 902 for taxes "deemed to have been paid" and 3) that in computing the indirect credit plaintiff is entitled to take into account, in addition to the proportionate part of the United Kingdom profits tax, a proportionate part of the standard tax which was paid by United Kingdom subsidiaries but was not

claimed, and could not be claimed by plaintiff as a credit under the Convention.

The Government contends that if a direct credit is claimed under the Convention by plaintiff for the standard tax "appropriate to" the dividend received from its United Kingdom subsidiaries, then no part of the standard tax paid by the subsidiaries can be included in the subsidiaries' creditable taxes in the computation of plaintiff's indirect credit under Section 902(a). Conversely, the Government argues that if any part of the standard tax paid by the United Kingdom subsidiaries was included in the subsidiaries' creditable taxes, as a tax paid by the subsidiaries in the computation of an indirect credit under Section 902(a), plaintiff cannot claim a direct credit under the Convention and Section 901(b) for that portion of the subsidiaries' standard tax which was "appropriate to" the dividend received by plaintiff from the subsidiaries.

DISCUSSION AND CONCLUSIONS OF LAW

This action concerns the interrelationship of the Convention, §§ 901(b) and 902(a) Internal Revenue Code of 1954, and the Supreme Court decision in *Biddle* v. *Commissioner*, 302 U.S. 573 (1938).

The purpose of foreign tax credit legislation is to prevent double taxation of foreign source income. *American Chicle Co.* v. *United States*, 316 U.S. 450 (1942); *Burnet* v. *Chicago Portrait Co.*, 285 U.S. 1 (1932); *Gentsch* v. *Goodyear Tire & Rubber Co.*, 151 F.2d 997 (C.A. 6 1945). The theory of the credit is well stated in Owens, *The Foreign Tax Credit* (Cambridge 1961) at pages 295-296:

> "A foreign tax credit system is a unilateral method of eliminating international double taxation of the nationals of a country which taxes its nationals on world-wide income. When United States nationals — citizens, domestic

corporations and residents – receive income from foreign countries, double taxation arises primarily because foreign countries assert tax jurisdiction on the grounds that the source of the income is in the foreign country while the United States asserts jurisdiction on the basis of nationality, i.e., the citizenship [or] residence of individuals and the place of incorporation of corporations, regardless of the source of the income. Since a tax is imposed both by the country of source of the income and the country of nationality, double taxation, or taxation of income by two countries, occurs * * *. It is clear, however, that if a country which taxes its nationals on income from all geographical sources decides to take unilateral action to relieve double taxation, it can do so only by allowing the country of source of the income the prior claim on that income. A complete shift to the principle of taxation only at source is unnecessary since the 'burden' of double taxation under a tax credit system is deemed to be only the excess taxation occurring when the taxpayer is subjected, because it pays taxes to more than one country, to an aggregate tax rate which exceeds the generally applicable rate of the crediting country. Consequently, the tax credit system is based on two principles: first, that the place of source has the first claim on the taxpayer's income and second, that the crediting country, as the country of nationality, may properly impose an additional tax to the extent income has not already been taxed at its source at a rate as high as that of the crediting country."

The stipulations, which the Court has adopted as its findings of fact, are sufficiently clear with respect to the manner in which the United Kingdom levies and collects taxes and the Court sees no need to amplify those facts.

The Government does not dispute plaintiff's contentions 1 and 2 above but with respect to 3 argues that since a direct credit was claimed for the standard tax "appropriate to" the dividend received from the United Kingdom subsidiaries, no

part of the standard tax paid by the subsidiaries could be included in plaintiff's creditable taxes in the computation of its indirect credit under § 902(a).

Prior to *Biddle* v. *Commissioner, supra,* the Internal Revenue Service treated American shareholders as the party paying the United Kingdom standard tax and allowed the shareholder to claim a direct credit for the tax. In *Biddle,* the Supreme Court held that the United Kingdom standard tax constituted a corporate tax which is imposed on the United Kingdom corporation paying the dividend and was not a tax on the shareholder who was the recipient of the dividend. Accordingly, the shareholder was not permitted to claim a direct credit for the tax.

Because the consequence of *Biddle* were believed to be harsh, the effect of that case was substantially altered by the Convention. Under the Convention, as amended, a recipient of a dividend paid by a United Kingdom corporation could, if he elected as provided for in the Convention, treat the standard tax appropriate to the dividends as if he had paid that tax and could therefore claim a direct credit for it, subject to the limitations of §§ 901-905 of the Internal Revenue Service as in effect on January 1, 1956.

Article XIII of the Convention, as amended, provided, in 1958 that:

> "(1) Subject to Sections 901 to 905 of the United States Internal Revenue Code as in effect on the 1st day of January 1956, United Kingdom tax shall be allowed as a credit against United States tax. For this purpose (a) the recipient of a dividend paid by a corporation which is a resident of the United Kingdom shall be deemed to have paid the United Kingdom tax appropriate to such dividend • • • if the recipient of the dividend • • • elects to include in his gross income for the purposes of United States tax the amount of such United Kingdom income tax."

The Convention makes no reference to the remaining standard tax, that is, the total standard tax paid by the subsidiary less the standard tax appropriate to the dividend received by plaintiff. Plaintiff therefore contends that the remaining standard tax should be treated as a corporate income tax paid by the United Kingdom corporations and treated in the same manner as the United Kingdom profits tax, the latter being admittedly proper for use in determining the credit available under § 902.

The Court agrees with plaintiff's contention. Article I of the Convention provides:

> "(1) The taxes which are the subject of the present are:
> • • • •
> (b) In the United Kingdom of Great Britain and Northern Ireland: The income tax (including surtax), the excess profits tax and the national defense contribution (hereinafter referred to as United Kingdom tax)
> • • • •"

and Article XIII, as amended, provides:

> "(1) Subject to Sections 901 to 905 . . . United Kingdom tax shall be allowed as a credit against United States tax. . . ."

The Court does not believe that the Convention contemplated that a part of the standard tax should be excluded from favorable tax treatment as an indirect credit under § 902. Article XIII does not say or imply that only a part of the United Kingdom tax should be allowed as a credit and the Court can find no reason for doing so.

Finally, the case of *United Shoe Machinery Corporation* v. *White*, 89 F.2d 363 (C.A. 1 1937) motion to modify denied, 91 F.2d 342 (1937) cert. denied 302 U.S. 768 (1937) relied upon by the Government is not analagous to the instant case.

In that case the Court stated "The plaintiff is thus claiming two deductions with reference to the same identical tax. . . ." The plaintiff in the instant action is not, as in the foregoing case, attempting to claim an indirect credit with respect to the standard tax "appropriate to" the dividend received, but is limiting the indirect credit to the remaining standard tax for which no direct credit has been claimed.

The Court concludes that the Question Presented as stated on page 19, must be answered "Yes."

ORDER

In accordance with the foregoing and applying the formula contained in *American Chicle Co.* v. *United States,* 316 U.S. 450 (1942) for determining the amount of indirect credit for the creditable foreign tax paid by the foreign corporations which the domestic corporation "shall be deemed to have paid" under § 902(a), the parties shall compute the amount of judgment to plaintiff and submit said computation for the Court's approval, accompanied with an entry of judgment.

It is so ORDERED.

/s/ Carl A. Weinman
Chief Judge U. S. District Court

(CAPTION OMITTED)

JUDGMENT

(Filed May 11, 1967)

The Court having considered the evidence and the arguments of counsel, and having entered its findings of fact and conclusions of law herein, it is in conformity therewith:

ORDERED, that plaintiff have judgment against defendant for the principal amount of $508,643.65 tax and $96,263.84 assessed interest, with interest thereon at six percent according to law.

DONE IN OPEN COURT at Dayton, Ohio, this 11th day of May, 1967.

/s/ Carl A. Weinman
Carl A. Weinman
Chief Judge,
United States District Court

Presented and approved by:

/s/ Phillip R. Becker
Phillip R. Becker
Cowden, Pfarrer, Crew and Becker

/s/ George W. Beatty
George W. Beatty
Lee, Toomey & Kent
Attorneys for Plaintiff

Approved as to form by:

/s/ Roger J. Makley
Roger J. Makley
United States Attorney

(CAPTION OMITTED)

ORDER AMENDING FINDINGS OF FACT

(Filed May 11, 1967)

Paragraph 17 of the Findings of Fact, filed by the Court on April 7, 1967, is amended (in accordance with the Amendment of Stipulation, filed by the parties on December 14, 1966) to read:

> "17. The credit under Section 901 computed by the Internal Revenue Service as stated in the preceding paragraph resulted in a smaller tax liability for the plaintiff for 1958 than if the Internal Revenue Service had included in the plaintiff's taxable income the standard tax 'appropriate to' the dividends received by the plaintiff from its United Kingdom subsidiaries, allowed a 'direct credit' in the amount of such standard tax under the Convention, and allowed 'indirect credits' computed under Section 902 using the formula stated in the preceding paragraph modified by substituting (a) the 'grossed up amount of the dividend' for 'dividend received by plaintiff' and (b) the 'taxes other than standard tax paid by subsidiary' for 'total taxes paid by subsidiary.'"

It is so ORDERED.

/s/ Carl A. Weinman
Carl A. Weinman
Chief Judge,
United States District Court

Assented to:

/s/ Phillip R. Becker
Phillip R. Becker
Cowden, Pfarrer, Crew & Becker

/s/ George W. Beatty
George W. Beatty
Lee, Toomey & Kent
Attorneys for Plaintiff

.....
United States Attorney

(CAPTION OMITTED)

NOTICE OF APPEAL TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

(Filed July 10, 1967)

Notice is hereby given that UNITED STATES OF AMERICA, defendant herein, hereby appeals to the United States Court of Appeals for the Sixth Circuit from the judgment herein, filed May 11, 1967 granting judgment against the defendant.

ROBERT M. DRAPER,
United States Attorney,

ROGER J. MAKLEY,
Asst. United States Attorney,
222 Federal Building,
Dayton, Ohio 45401

INDEX

	Page
Opinions below	1
Jurisdiction	1
Question presented	1
Treaty and statute involved	2
Statement	2
Argument	6
Conclusion	13
Appendix A	14
Appendix B	17

CITATIONS

Cases:

Abbot Laboratories International Co. v. *United States*, 160 F. Supp. 321, affirmed *per curiam*, 267 F. 2d 940 — 9

American Chicle Co. v. *United States*, 316 U.S. 450 — 4, 5, 6, 7, 9, 10

Biddle v. *Commissioner*, 302 U.S. 573 — 7

Burnet v. *Chicago Portrait Co.*, 285 U.S. 1 — 7

Treaties and Statutes:

Fourth Supplementary Protocol of March 17, 1966, 17 U.S. Treaties 1254, 1261–1262, Art. 9 — 13

Income Tax Convention between the United States and the United Kingdom, April 16, 1945, 60 Stat. 1377, as amended:

Art. I — 2, 14

Art. XIII — 2, 4, 5, 6, 7, 8, 11, 12, 13, 14

Internal Revenue Code of 1939, Sec. 131(a) (26 U.S.C. (1952 ed.) 131(a)) — 7

336-008—69——1

Treaties and Statutes—Continued
Internal Revenue Code of 1954: Page
Sec. 243 8
Sec. 245 8
Secs. 901–906 7
Sec. 901 10
Sec. 901(a) 2, 15
Sec. 901(b) 2, 7, 8, 12, 15
Sec. 902 4, 5, 6, 8, 9, 10, 12, 13
Sec. 902(a) 2, 16
Sec. 902(c) 2, 16
Sec. 904 10, 11
Sec. 904(a) 2, 16
Revenue Act of 1928, Sec. 131(a), 45 Stat. 829 7
Miscellaneous:
Alexander, *The Income Tax Convention with the United Kingdom,* 2 Tax L. Rev. 295 (1947) 12
Gordon, *Effect of Recent Treaty Changes on U.S. Taxation of Business Abroad,* 26 J. of Taxation 218 (1967) 13
Owens, *The Foreign Tax Credit* (1961) 6, 7
S. Exec. Rep. No. 4, 79th Cong., 2d Sess. (2 Leg. Hist. of Tax Conv. 2721) 12
S. Exec. Rep. No. 6, 79th Cong., 1st Sess. (2 Leg. Hist. of Tax Conv. 2651) 12
S. Exec. Rep. No. 3, 89th Cong., 2d Sess 13
Senate Hearings before a Subcommittee of the Committee on Foreign Relations on Conventions with Great Britain and Northern Ireland Respecting Income and Estate Taxes, 79th Cong., 1st Sess. (2 Leg. Hist. of Tax Conv. 2583) 12
Taxation in the United Kingdom, World Tax Series (Harv. L. School, 1957) 3

In the Supreme Court of the United States

OCTOBER TERM, 1968

No. 955

THE NATIONAL CASH REGISTER COMPANY, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINIONS BELOW

The opinion of the court of appeals (Pet. 1a–10a) is reported at 400 F. 2d 820. The opinion of the district court (R. 13a–32a) is reported at 270 F. Supp. 930.

JURISDICTION

The judgment of the court of appeals was entered on September 12, 1968, and the petition for rehearing was denied on October 23, 1968. (Pet. 11a.) The petition for a writ of certiorari was filed on January 18, 1969. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTION PRESENTED

Whether a credit for the United Kingdom standard (income) Tax paid by petitioner's British subsidiaries

may be claimed under both Article XIII of the Income Tax Convention with the United Kingdom and Section 902 of the Internal Revenue Code of 1954.

TREATY AND STATUTE INVOLVED

The pertinent parts of Articles I and XIII of the Income Tax Convention of April 16, 1945, between the United States and the United Kingdom, 60 Stat. 1377 (as amended by the Third Supplementary Protocol of August 19, 1957, 9 U.S. Treaties 1329, Art. II), and of Sections 901(a) and (b)(1), 902(a) and (c)(1), and 904(a) of the Internal Revenue Code of 1954 are set forth in Appendix A, *infra*.

STATEMENT

1. During 1958, the taxable year in question, petitioner, an American corporation, owned all of the voting stock of two subsidiary corporations, The National Cash Register Co., Ltd. and the National Cash Register (Manufacturing) Ltd. Both of these subsidiaries were organized under the laws of the United Kingdom. (Pet. 1a.)

As British corporations, both of petitioner's subsidiary corporations were subject to the then applicable United Kingdom standard tax on income imposed at the flat rate of 38.75 per cent on corporations and individuals, and a profits tax, applicable only to corporations, at the rate of 10 percent. Both the standard tax and the profits tax were imposed on a resident corporation's net earnings for the taxable year, without deduction for any dividends declared

from such earnings; neither tax was deductible in computing the other. (Pet. 3a; R. 16a.) [1]

In 1958, petitioner received $2,591,171 in dividends "free of standard tax" and $1,693,857 in other income from its two wholly owned British subsidiaries. In that year, these subsidiaries paid $2,667,233 in standard tax and $542,976 in profits tax to the United Kingdom. (R. 14a–15a, 18a.)

During the year in question, a corporation residing in the United Kingdom could declare dividends either "free of standard tax" or "with deduction of standard tax." When dividends were paid "free of standard tax," as they were here, the declared amount of the dividend is actually paid to the shareholder and the dividend is not subject to any additional United Kingdom standard tax after it has been paid to the shareholder. For British tax purposes other than the assessment of standard tax, the shareholder is required to include the so-called "grossed-up" dividend in income.[2] This is the amount of the dividend actually received, plus the amount of the standard tax rate effective at the time of distribution. (R. 16a–17a, 18a.) [3]

2. In its United States 1958 tax returns petitioner chose to compute a foreign tax credit for the stand-

[1] "R." references are to the separately bound Appendix C to the petition.

[2] A detailed explanation of the United Kingdom Tax treatment of dividends appears in *Taxation in the United Kingdom*, World Tax Series (Harv. L. School, 1957) pp. 255–258.

[3] As the Sixth Circuit noted (Pet. 4a, n.6):

> If a British corporation declared a dividend of $6.00 "free of standard tax" and if the standard tax were im-

ard tax paid by its subsidiaries under Article XIII of the Income Tax Convention between the United States and the United Kingdom. It included in its taxable United States income $4,230,483.68, which represented the dividend declared and received in the amount of $2,591,171.26 plus the standard tax "appropriate to" the dividend in the amount of $1,639,-312.42. In addition to the $1,639,312.42 foreign tax credit claimed under the treaty, petitioner claimed a further credit under Section 902 of the 1954 Internal Revenue Code in the amount of $1,035,313.09, which consisted of $362,497.67 for the profits tax, $3,508.85 for the miscellaneous foreign taxes, and $669,306.57 for a portion of the remaining standard tax paid by their subsidiaries.[4] (R. 22a–24a.)

---

posed at the rate of 40 per cent, the shareholder would have to report $10.00, representing $6.00 for the dividend received and $4.00 for the standard tax appropriate to the dividend.

This example does not take into account the 10% profits tax. If a corporation had a profit of $10, the accumulated (after-tax) profits would be $5. If the entire $5 were distributed as a dividend, the standard tax appropriate to the dividend would be $3.33. The British shareholder never takes into income the $0.67 in standard tax appropriate to the $1 profits tax. For the purposes of this case $5,081 in other foreign income taxes may be treated in the same way as the profits tax. (R. 15a; Pet. 5, n.2; 6a, n.8.)

[4] Taxpayer made an alternative claim for a portion of the remaining standard tax in the amount of $444,746.80. (R. 24a.) To arrive at these figures, computations under the *American Chicle* formula (see footnote 7, *infra*) for the profits tax and the miscellaneous foreign taxes were made separately for each of petitioner's subsidiaries. The resulting amounts for the credits for the profits tax and miscellaneous taxes were added together and then subtracted from the total indirect credit claimed by petitioner for its subsidiaries to obtain the amount claimed

The Commissioner of Internal Revenue disallowed the claimed credits on the ground that credit for the standard tax may be taken either under Article XIII or under Section 902, but not under both. The Service recomputed the credits using two alternative methods: first, using Article XIII for the standard tax and Section 902 for the other taxes; and second, using Section 902 for all taxes. Under the first method, the amount of the credit allowed was $2,005,318.94,[5] with a resulting United States tax liability of $194,532.55.[6] Under the second method used, the credit as computed under the *American Chicle* formula[7] was $1,313,-539.40, which included $1,089,357.57 for the standard tax, $222,032.66 for the profits tax, and $2,149.17 for the miscellaneous foreign taxes. (R. 25a–26a.) The resulting United States tax liability on the dividends

---

for the portion of the remaining standard tax. Petitioner's formulas for arriving at the total credit claimed under Section 902 are set forth at R. 23a, 24a. In making the computations throughout this brief it is necessary to treat each of petitioner's subsidiaries separately before the total amounts can be determined.

[5] The sum was derived by subtracting the portion of the remaining standard tax claimed by petitioner from its total credit.

[6] To reach this amount, subtract the foreign tax credit from the United States income tax before foreign tax credit under taxpayer's original computation. See Appendix B, *infra*.

[7] *American Chicle Co.* v. *United States*, 316 U.S. 450:

$$\frac{\text{Dividend received by petitioner}}{\text{subsidiary's "Accumulated profits"}} \times \frac{\text{subsidiary's "Accumulated profits"}}{\text{subsidiary's "Total profits"}} \times \text{Total foreign creditable taxes paid by subsidiary} = \text{Credit}$$

received from its British subsidiaries was $33,869.65.[8] (The computations are set forth in detail in Appendix B, p. 17, *infra*). A deficiency was asserted on the basis of the latter computation, since it yielded the smaller tax liability (R. 13a–14a, 25a–26a, 34a).

Petitioner paid the deficiency and instituted this action upon the denial of its refund claim. (R. 13a–14a.) The district court sustained petitioner's computation. (Pet. 7a; R. 28a–32a.) Upon appeal by the government, the court of appeals reversed, holding that petitioner must compute its credit for standard tax under either Article XIII or Section 902, but not under both.

ARGUMENT

The decision below is correct. There is no conflict among the circuits or any other basis for further review.

---

[8] In this case there are two reasons why it is advantageous for the petitioner to compute its foreign tax credit under Section 902. First: unlike the direct credit situation (*e.g.*, under Article XIII of the Treaty) where the total income before foreign tax is included in gross income for United States tax purposes and a credit is allowed equal to the amount of the foreign tax paid on the amount included in gross income at the statutory foreign tax rate, under Section 902 only foreign income after foreign tax is included in United States gross income and a credit is allowed for the foreign tax paid on the accumulated profits distributed as dividends. Thus, both a deduction and a credit is afforded for foreign taxes. The result is an aggregate tax rate that may be less than the 52 percent United States tax rate. Second, when "total profits" as used in the *American Chicle* formula do not equal the British taxable income on which the standard tax is imposed, the effective standard tax rate may be greater (as is the case here) under Section 902 than the statutory foreign standard tax rate. See Owens, *The Foreign Tax Credit* (1961) pp. 113–118, 125–126.

1. In order to eliminate double taxation by assuring as nearly as possible that income subject to tax in both the United States and a foreign country is taxed at no more than the higher of either the United States or foreign rate,[9] Sections 901–906 of the Internal Revenue Code of 1954 allow American taxpayers to claim credit for foreign taxes if specified conditions are met. The basic provision applicable here is Section 901(b)(1), which provides that "a domestic corporation" may have a credit, subject to limits established in Section 904, for "the amount of any income, war profits, and excess profit taxes paid or accrued during the taxable year to any foreign country * * *." This provision, however, speaks only in terms of taxes the American taxpayer has paid directly to foreign governments. Thus, in *Biddle* v. *Commissioner,* 302 U.S. 573, this Court, in interpreting the predecessor provision to Section 901(b)(1),[10] held that an American shareholder of a British corporation could not claim a credit for the British standard tax paid by the corporation, even though the shareholder's "grossed-up" dividend included a ratable portion of the standard tax paid by the corporation.

This rule was modified, however, by Article XIII of the Income Tax Convention of April 16, 1945, between the United States and the United Kingdom, 60 Stat. 1377. Section (1)(a) of that Article pro-

[9] *Burnet* v. *Chicago Portrait Co.*, 285 U.S. 1, 8; *American Chicle* v. *United States*, 316 U.S. 450, 451; Owens, *The Foreign Tax Credit* (1961), pp. 3, 113, 295–296.

[10] Section 131(a) of the Revenue Act of 1928; see, also, Section 131(a) of the Internal Revenue Code of 1939.

vides that "the recipient of a dividend paid by a corporation which is a resident of the United Kingdom shall be deemed to have paid the United Kingdom tax appropriate to such dividend * * *." As a result, an American shareholder of a British corporation is allowed to claim a credit under Section 901(b)(1) of the 1954 Code to the same extent as he could if he had paid the standard tax "appropriate to" his dividend directly to the British government.

A different type of foreign tax credit is generally allowed by Section 902. This provision is an analogue to the dividend received deduction that Sections 243 and 245 of the 1954 Code allow a domestic corporation. Section 902 applies only to domestic corporations which own at least 10 per cent of the voting stock of a foreign corporation. Once that minimum shareholding percentage is met, the American corporation is "deemed" to be the payor of the fraction of the foreign taxes that the subsidiary paid "on or with respect to [the] * * * accumulated profits" from which the dividends were paid.

It is readily apparent that Article XIII and Section 902 each provide relief in the same general set of circumstances—the payment of a dividend by a British corporation to an American shareholder. Section 902 applies only when the shareholder is an American corporation owning at least 10 per cent of the voting stock in the British corporation, while Article XIII is available to any American national regardless of the extent of his stockholdings. In each situation the respective provision holds that the American tax-

payer is "deemed" to have paid the foreign tax that was in fact paid by the British corporation.

If the conditions of Section 902 are met, there is an obvious overlap between it and Article XIII of the Convention. Each provision applies only when in fact a dividend has been paid to the American shareholder. *Abbot Laboratories International Co.* v. *United States,* 160 F. Supp. 321, 328 (N.D. Ill.), affirmed *per curiam,* 267 F. 2d 940 (C.A. 7); see, also, *American Chicle Co.* v. *United States,* 316 U.S. 450, 452. In either case, the credit is limited to the ratable portion of the British tax attributable to the dividend received by the American shareholder.

Petitioner seeks to take advantage of the overlap between these provisions by claiming both a credit under the treaty for the British standard tax appropriate to the dividends received by it and reported in its United States taxable income and a credit under Section 902 for a portion of the remaining standard tax paid by its subsidiaries in the amount of $669,306.57 (or under its alternative claim of $444,746.90). (R. 23a, 24a.) The treaty, however, allows petitioner credit for the full amount of the standard tax attributable to the distributed part of the subsidiaries' profits. The remaining amount of the standard tax—*i.e.,* the amount for which petitioner claims credit under Section 902—is attributable to monies that were not distributed as dividends but were instead retained as undistributed accumulated profits[**] or used to pay

[**] Petitioner's subsidiaries distributed only 5% of their accumulated profits (R. 15a, 18a).

the British profits tax.[12] Thus petitioner seeks to misuse Section 902 by obtaining a credit for British taxes attributable to amounts not paid to it as a dividend, contrary to the express language of Section 902.

2. Petitioner's case is not advanced, as it suggests, by the fact that Section 904 is no bar to the credit claimed (Pet. 5, 18; R. 27a). That provision limits the amount of the foreign tax credit allowable under the direct and indirect credits to "the same proportion of the tax against which such credit is taken [*i.e.*, before-credit United States tax] which the taxpayer's taxable income from sources within such country * * * bears to his entire taxable income." Thus, the credit may in no event exceed the pre-credit United States tax on the foreign income.

The Section 904 limitation thus establishes a maximum credit that may be claimed, but offers no additional credit when the credit allowable under Sections 901 and 902 is less than the maximum. In addition, the only reason petitioner's computation suggests compliance with Section 904 is because it assumes that the limitation is based on the pre-credit United States tax due on petitioner's total United Kingdom income, which includes not only the dividends but $1,693,857 in other income (Pet. 7a). If the other income is eliminated, then the maximum credit allowable under

[12] No credit is available for the amount of standard tax appropriate to the amounts used to pay British profits tax. See *American Chicle*, *supra*, 316 U.S. at 452. Here, the subsidiaries used more than $540,000 (R. 15a) of their pre-tax earnings, which were subject to standard tax, to pay the profits tax, which was not deductible for the purposes of the standard tax (R. 15a, 16a).

Section 904—the pre-credit United States tax on the dividends—would be $2,199,851, considerably less than the credit of $2,674,625 which petitioner claims. See Appendix B, *infra,* lines (d) and (f). On the other hand, the credit of $1,313,539 approved by the Sixth Circuit would be slightly less than the before-credit tax liability of $1,347,409,[13] producing a federal tax liability on the dividends of $33,869. Appendix B, p. 17, *infra,* lines (d), (g), and (h). This result—and not petitioner's—comports with the foreign tax credit's purpose of insuring that foreign profits are taxed at the higher of the foreign rate or the United States rate. Since the aggregate British tax rate, approximately 50%,[14] is less than the United States rate for 1958 of 52%, a small federal tax should be due on the dividends. The real effect of petitioner's computation is to generate excess tax credits large enough to eliminate any federal tax on the dividends and to reduce significantly the federal tax due on the other income. Appendix B, *infra,* lines (j) and (k).

3. The decision of the court of appeals is neither inconsistent with *Biddle* nor does it deny petitioner any benefit accorded by the treaty. (See Pet. 7, 15–16, 19–20.) The purpose of Article XIII, which was part

[13] The difference between the before-credit tax liabilities computed under petitioner's theory and under the court of appeals' holding is due to petitioner's inclusion in income of the standard tax appropriate to the dividends. Appendix B, *infra*, line (b), p. 17.

[14] The United Kingdom standard tax is 38.75% and the profits tax 10% and since neither is deductible in computing the other, the aggregate rate is approximately 50%. We include in this figure the miscellaneous foreign income taxes. (R. 15a, 16a.)

of the settlement of the broader problem of the taxation of dividend income by both signatories, was to afford relief from the principle of the *Biddle* case, and it enables shareholders not qualifying for the indirect credit of Section 902 to take a credit for standard tax under Section 901(b).[16] But Article XIII expressly states that it is "Subject to Sections 901 to 905 of the United States Internal Revenue Code". There is no basis in the treaty or in *Biddle* for applying Section 902 to any amount of British standard tax except that allocable to the dividends in fact paid to petitioner. Since that amount of standard tax is covered by the treaty, the case must yield to the rule that requires a taxpayer to choose among duplicative tax benefits, and the Sixth Circuit's decision to this effect contains no infringement of Article XIII.

The treaty does no more than grant corporate shareholders relief as an alternative to a credit under Section 902.[17] While Section 902 ordinarily provides a greater tax benefit than does Article XIII, there are circumstances in which the reverse is true.[18] Consequently, by allowing corporate 10 per cent sharehold-

[15] [16] Senate Hearing before a Subcommittee of the Committee on Foreign Relations on Conventions with Great Britain and Northern Ireland Respecting Income and Estate Taxes, 79th Cong., 1st Sess., pp. 60, 70–71, 77 (2 Leg. Hist. of Tax Conv. 2583, 2626, 2636–2637, 2643); S. Exec. Rep. No. 4, 79th Cong., 2d Sess., p. 18 (2 Leg. Hist. of Tax Conv. 2721, 2738); Alexander, *The Income Tax Convention with the United Kingdom*, 2 Tax L. Rev. 295, 322–325 (1947).

[16] [17] See Technical Memorandum of the Treasury Department on the Convention (S. Exec. Rep. No. 6, 79th Cong., 1st Sess., pp. 5, 11).

[17] [18] Owens, *The Foreign Tax Credit* (1961), pp. 370–372.

ers a choice between Section 902 and Article XIII, the negotiators insured that such shareholders would not lose the benefits previously accorded them and yet would have at least the same relief which Article XIII provides to other shareholders.

4. The issue presented is of limited future importance. In 1965, the United Kingdom eliminated the standard tax and adopted separate corporate and individual income taxes, and Article XIII was then extensively changed.[18] The Internal Revenue Service advises that the issue is presently pending in one case in the Court of Claims and in seven cases at the administrative level, involving claims of $3,734,138 in total.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

ERWIN N. GRISWOLD,
Solicitor General.

JOHNNIE M. WALTER,
Assistant Attorney General.

STUART A. SMITH,
DAVID ENGLISH CARMACK,
Attorneys.

MARCH 1969.

---

[18] Fourth Supplementary Protocol of March 17, 1966, 17 U.S. Treaties 1254, 1261–1262, Art. 9; Exec. Rep. No. 3, 89th Cong., 2d Sess., pp. 5, 33–34, 47–50; Gordon, *Effect of Recent Treaty Changes on U.S. Taxation of Business Abroad*, 26 J. of Taxation 218 (1967).

APPENDIX A

Income Tax Convention of April 16, 1945, between the United States and the United Kingdom, 60 Stat. 1377 (as amended by the Third Supplementary Protocol of August 19, 1957, 9 U.S. Treaties 1329, Art. II):

ARTICLE I

(1) The taxes which are the subject of the present Convention are:

(a) In the United States of America: The Federal income taxes, including surtaxes and excess profits taxes (hereinafter referred to as United States tax).

(b) In the United Kingdom of Great Britain and Northern Ireland: The income tax (including surtax), the excess profits tax and the national defense contribution (hereinafter referred to as United Kingdom tax).

(2) The present Convention shall also apply to any other taxes of a substantially similar character imposed by either Contracting Party subsequently to the date of signature of the present Convention or by the government of any territory to which the present Convention is extended under Article XXII.

* * * * *

ARTICLE XIII

(1) Subject to Sections 901 to 905 of the United States Internal Revenue Code as in effect on the 1st day of January 1956, United

Kingdom tax shall be allowed as a credit against United States tax. For this purpose

(a) the recipient of a dividend paid by a corporation which is a resident of the United Kingdom shall be deemed to have paid the United Kingdom tax appropriate to such dividend, and

(b) the recipient of any royalty or other amount coming within the scope of Article VIII of the present Convention shall be deemed to have paid any United Kingdom tax legally deducted from the royalty or other amount by the person by or through whom any payment thereof is made,

if the recipient of the dividend or royalty or other amount, as the case may be, elects to include in his gross income for the purposes of United States tax the amount of such United Kingdom income tax.

Internal Revenue Code of 1954:

SEC. 901. *Taxes of Foreign Countries and of Possessions of United States.*

(a) *Allowance of Credit.*—If the taxpayer chooses to have the benefits of this subpart, the tax imposed by this chapter shall, subject to the limitation of section 904, be credited with the amounts provided in the applicable paragraph of subsection (b) plus, in the case of a corporation, the taxes deemed to have been paid under section 902 * * *.

(b) *Amount Allowed.*—Subject to the limitation of section 904, the following amounts shall be allowed as the credit under subsection (a):

(1) *Citizens and Domestic Corporations.*—In the case of a citizen of the United States and of a domestic corporation, the amount of any income, war profits, and excess profits taxes paid or accrued during the taxable year to any foreign country or to any possession of the United States;

* * * * *

[26 U.S.C. (1958 ed.) 901.]

SEC. 902. *Credit for Corporate Stockholder in Foreign Corporation.*

(a) *Treatment of Taxes Paid by Foreign Corporation.*—For purposes of this subpart, a domestic corporation which owns at least 10 percent of the voting stock of a foreign corporation from which it receives dividends in any taxable year shall be deemed to have paid the same proportion of any income, war profits, or excess profits taxes paid or deemed to be paid by such foreign corporation to any foreign country or to any possession of the United States, on or with respect to the accumulated profits of such foreign corporation from which such dividends were paid, which the amount of such dividends bears to the amount of such accumulated profits.

* * * * *

(c) *Applicable Rules.*—

(1) The term "accumulated profits," when used in this section in reference to a foreign corporation, means the amount of its gains, profits, or income in excess of the income, war profits, and excess profits taxes imposed on or with respect to such profits or income * * *.

* * * * *

[26 U.S.C. (1958 ed.) 902.]

SEC. 904. *Limitation on Credit.*

(a) *Limitation.*—The amount of the credit in respect of the tax paid or accrued to any country shall not exceed the same proportion of the tax against which such credit is taken which the taxpayer's taxable income from sources within such country (but not in excess of the taxpayer's entire taxable income) bears to his entire taxable income for the same taxable year.

[26 U.S.C. (1958 ed.) 904.]

APPENDIX B

The differences between the taxpayer's original computation of its foreign tax credit for 1958, its alternative computation, and the computation made by the Internal Revenue Service are shown by the following table:

	Taxpayer's Original Computation (R. 22a-23a)	Taxpayer's Alternative Computation (R. 23a-24a)	Internal Revenue Service's Computation (R. 25a-26a)
Taxpayer's U.S. taxable income from its U.K. subsidiaries also subject to creditable foreign taxes:			
(a) Dividends (R. 18a)	$2,591,171.26	$2,591,171.26	$2,591,171.26
(b) Standard tax "appropriate to" dividends (R. 18a)	$1,639,312.42	$1,639,312.42	
(c) Total	$4,230,483.68	$4,230,483.68	$2,591,171.26
U.S. income tax, before foreign tax credit, on income also subject to creditable foreign taxes:			
(d) 52% of line (c)	$2,199,851.51	$2,199,851.51	$1,347,409.05
Taxpayer's foreign tax credit under Sec. 901 (without regard for limitation under Sec. 904):			
(e) Computed under Sec. 901(b) and the Convention (R. 22a-24a)	$1,639,312.42	$1,639,312.42	
(f) Computed under Sec. 902(a) (R. 22a-26a)	$1,035,313.09	$ 810,753.42	$1,313,539.40
(g) Total	$2,674,625.51	$2,450,065.84	$1,313,539.40
U.S. income tax, after foreign tax credit, on income also subject to creditable foreign taxes:			
(h) line (d) minus line (g)	($ 474,774.00)	($ 250,214.33)	$ 33,869.65
(i) (R. 18a)	$1,693,857.13	$1,693,857.13	$1,693,857.13
U.S. income tax on income not also subject to creditable foreign taxes:			
(j) 52% of line (i)	$ 880,805.70	$ 880,805.70	$ 880,805.70
U.S. income tax, after foreign tax credit, on taxpayer's total income from its U. K. subsidiaries:			
(k) line (h) minus line (j)	$ 406,031.70	$ 630,591.37	$ 914,675.35

The amount of income taxes involved in this case is the difference between the taxpayer's liability (line k) as computed by the Internal Revenue Service ($914,675.35) and as computed by the taxpayer under its original computation ($406,031.70) and its alternative computation ($630,591.37).

U.S. GOVERNMENT PRINTING OFFICE: 1969